Supreme Court of the United States

OCTOBER TERM, 1942

In the Matter
of
THE WESTERN PACIFIC RAILROAD COMPANY, *Debtor.*

FREDERICK H. ECKER, *et al., Petitioners,* *v.* WESTERN PACIFIC RAILROAD CORPORATION, *et al., Respondents.*	No. 7
CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO and SAMUEL ARMSTRONG, *Petitioners,* *v.* WESTERN PACIFIC RAILROAD CORPORATION, *et al., Respondents.*	No. 8
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IRVING TRUST COMPANY, *Petitioner,* *v.* CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO, *et al., Respondents.*	No. 61

BRIEF ON BEHALF OF A. C. JAMES CO., RESPONDENT

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SUBJECT INDEX

INDEX TO APPENDIX

TABLE OF CASES

INTERSTATE COMMERCE COMMISSION REPORTS

TEXT BOOKS AND PERIODICALS

STATUTES[1]

[1]Citations to Section 77 of the Bankruptcy Act are too frequent for enumeration. Substantially all of the statute is reprinted in the appendix to this brief at pages i to xxvi.

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BRIEF ON BEHALF OF A. C. JAMES CO., RESPONDENT

Introductory

A. C. James Co. has a secured claim against the debtor railroad in the principal amount of $4,999.80, which claim is described more fully at page 10 of this brief. This

Note: All emphasis in quoted matter has been supplied throughout this brief unless otherwise indicated.

claim was classified as a separate class of creditor, under subsection (c)(7) of Section 77 of the Bankruptcy Act, by order of the District Court dated August 20, 1935 (R. 1023).

In the pending proceeding under Section 77 of the Bankruptcy Act the Interstate Commerce Commission rejected three plans of reorganization filed by parties to the proceeding, and several amended plans, in all of which provision was made for refunding in full the secured claim of this respondent. The Commission then formulated, and in this proceeding seeks to impose upon the creditors, under claimed authority of Section 77, its own plan of reorganization, which is here in issue. This Commission Plan has the effect of disregarding, cancelling, and refusing to refund more than half of the secured claim of A. C. James Co.

A. C. James Co. has contended below, and will urge in this Court, that nothing in the facts, or in Section 77 of the Bankruptcy Act, or in the law of the land, warrants or supports this confiscatory treatment of its secured claim.

This case brings before this Court something more than matters of procedural due process. It necessarily involves questions as to basic principles of administrative law, the relative functions of the courts and administrative agencies and the essential judicial function of construing the scope of powers delegated by Congressional act. The sound development of administrative law requires that an administrative agency shall function within the legislative mandate and seek to attain the legislative objectives. When an administrative agency—no matter how well-intentioned—goes outside the four corners of the statute, even as it may be clarified by any extrinsic indication of Congressional intent, and seeks to accomplish objectives not within the declared legislative purposes, those purposes are defeated. We maintain that the plainly indicated objects of the statute would be nullified by the Interstate Commerce Commission's interpretation of Section 77 of the Bankruptcy Act in this proceeding, and a

soundly conceived statute rendered in large part ineffective.

This is a case of novel impression in this Court. It involves the interpretation and application of Section 77 of the Bankruptcy Act (47 Stat. 1474, as amended; 11 U. S. C. A., § 205; all pertinent portions printed in full at pages i to xxvi of the appendix to this brief). Although Section 77 of the Bankruptcy Act was enacted in 1933 and substantially amended in 1935 to its present form (49 Stat. 1969), this is the first case in which the broad questions of the construction of Section 77 and its application to the reorganization of railroads has come before this Court.

In *Continental Illinois National Bank and Trust Company* v. *Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648, this Court sustained Section 77 of the Bankruptcy Act, in its general scope and aim, as within the power conferred on Congress by the bankruptcy clause of the Constitution. That case raised specifically the question of the jurisdiction of the bankruptcy court to enjoin creditors from selling their collateral during the pendency of a reorganization proceeding under Section 77, and this Court had no occasion to consider the questions of construction of the Section and its application which are raised in the present proceeding.

Opinions below

Opinion of Circuit Court of Appeals, 9th Circuit, 124 F. (2d) 136 (R. 2663);

Opinion of District Court, Northern District of California, Southern Division, 34 F. Supp. 493 (R. 1569);

Original Report and Order of Interstate Commerce Commission on October 10, 1938, 230 I. C. C. 61 (R. 194);

Commission's Modifying Report and Order, June 21, 1939, 233 I. C. C. 409 (R. 300).

Jurisdiction

The jurisdiction of this Court has been invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 [28 U. S. C. A., § 347 (a)] and § 24(c) of the Bankruptcy Act [11 U. S. C. A., § 47(c)]. The decree of the Circuit Court of Appeals for the Ninth Circuit was entered November 28, 1941 (R. 2675-6).

Scope of Review

The decision of the Circuit Court of Appeals for the Ninth Circuit, here under review, reversed an order entered by the District Court for the Northern District of California, Southern Division, on August 15, 1940. The order of the District Court had approved a plan of reorganization for the debtor railroad which had been promulgated by the Commission and certified to the District Court. The decision of the Circuit Court of Appeals was based substantially upon two grounds: (a) that the Commission and the District Court had failed to make the necessary findings of fact upon which the fairness and equity of the plan of reorganization could be judicially determined; and (b) that the District Court had misconstrued and improperly limited its judicial functions and duties under Section 77 of the Bankruptcy Act.

In this brief, this respondent will present for this Court's consideration, not merely the defects of procedural due process which the Circuit Court of Appeals quite properly found in the proceedings before the Commission and in the District Court, but substantial questions at issue in this proceeding involving the basic construction of Section 77 of the Bankruptcy Act.

It has seemed to us that in giving consideration to the matters specifically decided by the Circuit Court of Ap-

peals for the Ninth Circuit, this Court will also have to review at this time basic questions as to the construction and application of Section 77 of the Bankruptcy Act. The procedural defects found by the Circuit Court of Appeals in the proceedings below are rooted deep in basic misconstructions of Section 77 which were adopted by the Commission and by the District Court.

It should be noted in this connection that this Court has granted in this proceeding four petitions for certiorari and a cross-petition, without express limitation, which on their face raise issues which go considerably beyond the somewhat narrow bases of decision set out in the opinion of the Circuit Court of Appeals.

Moreover, the Commission has filed in this proceeding a memorandum *amicus curiae* in which it states that:

> "* * * it is important to the efficient performance of the Commission's duties under Section 77 that the procedure to be followed and the findings to be made by the Commission should be established by a definitive decision of this Court."

The Commission has thus expressed formally its desire that this Court indicate in its decision in this proceeding any basic errors in the construction and application of Section 77 which may appear from the Court's review of the proceeding, in order that the Commission may perform effectively the duties imposed upon it by Section 77, in the light of conditions then existing, when this case is returned to it for further consideration. *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134.

It must be admitted that under the procedure provided by Section 77 of the Bankruptcy Act the parties will have a later opportunity to bring up for review substantial questions of the construction of Section 77 which affect their interests. The plan of reorganiza-

tion which the Commission seeks to impose upon the creditors in this proceeding has not yet been submitted to the creditors for the required vote of approval under subsection (e) of Section 77. The only creditors (excluding the First Mortgage Trustees,[1] who have definitely aligned themselves with the insurance company bondholders, although they represent a minority of the outstanding bonds) now supporting the Commission Plan are (a) a group of insurance companies and one bank, functioning under the exception proviso of subsection (p) of Section 77, holding a little more than one-third of the First Mortgage Bonds of the debtor, and (b) the Reconstruction Finance Corporation, which is given under the Commission Plan a substantial and unwarranted preference as against other secured creditors. It may fairly be assumed that any plan formulated by the Commission, under what we deem to be its erroneous construction of Section 77, would not receive an affirmative vote of acceptance by all classes of secured creditors.

Under the express provisions of subsection (e) of Section 77 such plan might be confirmed by the District Court after an adverse vote by one or more classes of creditors, "if he [the District Judge] is satisfied and finds, after hearing, that it [the plan] makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; **that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts;** and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e)." Any such confirmation by the District Judge (assuming that any judge would make the required findings in the face of the demonstrated present day earning power of the debtor's railroad system) would be the subject of

[1] Subsection (c)(7) of Section 77, which permits mortgage trustees to file claims, expressly provides:

> "* * * nothing herein shall constitute such trustee or trustees the representative or representatives of such holders (bondholders) for the purpose of accepting or rejecting any plan of reorganization."

judicial review under the express provisions of subsection (f) of Section 77.

However, despite the existence under the procedure provided by the statute of a later opportunity to bring up additional questions for review, the time elements are such that all parties to this proceeding have a vital interest in a final determination, at this time, of these basic problems of construction and interpretation of Section 77.

Unless this Court does consider broadly the questions as to the proper construction of Section 77 of the Bankruptcy Act raised in this proceeding and hand down a final and definitive interpretation of that statute, it may be years before the reorganization of the debtor railroad can be completed. This may be sufficiently indicated by reference to the condensed chronological summary of the prior proceedings herein set forth below.

Chronological Summary of Proceedings Heretofore Had

August 2, 1935	Debtor's petition for reorganization filed with District Court and Commission and approved by District Court (R. 4, 1019).
August 20, 1935	Claims of creditors and stockholders classified by order of District Court (R. 1022).
February 8, 1936	Plan of reorganization filed by debtor with Court and Commission (R. 19).
March 23, 1936	Hearings before examiners of Commission commenced.
September 28, 1936	Plan of reorganization filed with Commission by Institutional Bondholders Committee (R. 48).
October 26, 1936	Plan of reorganization filed with Commission by A. C. James Co. (R. 101).

August 1, 1937	Proposed report issued by Bureau of Finance of Commission, rejecting plans submitted by the parties and promulgating Commission Plan (R. 116).
November 17, 1937	Hearing before Commission on exceptions to proposed plan filed by all parties to proceeding.
October 10, 1938	Commission issued original report and order approving Bureau of Finance Plan with some modification (R. 194, 281).
January 20, 1939	Hearing held before Commission on petitions of all parties for rehearing and modification.
June 21, 1939	Commission issued its "report and order on further consideration" approving modified plan of reorganization, modifying its report of October 10, 1938, and revoking order of that date (R. 300, 382).
September 28, 1939	Proceedings before Commission certified to District Court.
December 8, 1939	Objections to Commission Plan filed by this respondent and others in District Court (R. 892, et seq.).
January 22-25, 1940	Hearings before District Court.
August 15, 1940	Order entered by District Court overruling objections and approving Commission Plan (R. 1600).
July 28-29, 1941	Hearing on appeals in Circuit Court of Appeals.
November 28, 1941	Decree of Circuit Court of Appeals entered.
April 27, 1942	Petitions for certiorari and cross-petition granted by this Court.

For the reasons indicated above and in the interest of substantial justice, it therefore appears that the basic questions of the construction and application of the statute to the facts of this case, as well as the particular points of administrative and judicial procedure, are properly to be considered for decision by the Court at this time.

This brief is therefore directed, in substantial part, to the basic questions as to the construction of Section 77 and its application to the facts here before the Court. This respondent will file, prior to the argument, pursuant to the stipulation of the parties of August 15, 1942, a reply brief dealing specifically with such contentions of the petitioners as do not fall within the scope of the affirmative presentation adopted in this brief.

Statement of the Case

This respondent has contended throughout this proceeding that the claim of a secured creditor cannot, under Section 77 of the Bankruptcy Act lawfully be refused refunding in whole or part, and thus foreclosed, on the basis of a bald limitation of capitalization, utterly unrelated to the value as previously found by the Commission, of the properties of the debtor upon which the secured creditor holds a lien. The Commission and the District Court rejected this contention; the Circuit Court of Appeals has sustained it.

This respondent has also contended throughout this proceeding that the value of the debtor's railroad system, as it exists today, provides ample margin for the full recognition and refunding of respondent's secured claim; and that the Commission's prior valuation (under Section 19a of the Interstate Commerce Act, 49 U. S. C. A. Section 19a), as previously determined and reported in this proceeding, should not be materially diminished or otherwise modified

under the valuation provisions of subsection (e) of Section 77, if soundly construed.

In order that the factual background against which the legal questions arise may be clear to the Court, and in order to correct some possible misapprehensions which might flow from the manner of presentation of this factual background in the briefs of the petitioners, it seems desirable to present at this point a brief summary of the facts as to the claim of this respondent and as to the debtor's status.

Secured claim of A. C. James Co., this respondent

A. C. James Co. is a secured creditor of the debtor in the principal amount of $4,999,800, with unpaid accrued interest thereon at 5% per annum, from January 1, 1934. The aggregate debt, principal and interest, owing to A. C. James Co. on January 1, 1939, the effective date of the Commission Plan, was $6,249,750 (R. 1023).

This indebtedness arose from the purchase in 1931 and 1932 by A. C. James Co., at public sale, for cash, at full face value, of debentures of the debtor, authorized by the Interstate Commerce Commission in proceedings under Section 20a of the Interstate Commerce Act, to enable the debtor to complete its Northern California Extension, a connection with the Great Northern Railway, which Extension is now a substantial and highly important part of the debtor's railway system. In the indenture under which these debentures were issued, the debtor agreed that no new mortgage or pledge of the properties of the debtor would be created without calling these debentures for payment (I. C. C. Exhibit No. 50, p. 32).[1]

The report of the Commission dated November 20, 1930, approving the issue of these debentures, is printed in full in the appendix to this brief at pages xxvii to xxix (R. 2324).

[1] Admitted at R. 2335. Not printed in the Record by stipulation (R. 2616); original exhibit before this Court pursuant to stipulation filed July 23, 1942.

Subsequently in March and May, 1932, the debentures held by this respondent were exchanged for promissory notes of the debtor secured by its General and Refunding Mortgage bonds (R. 1084-6). The reports of the Commission providing for this exchange are a part of the unprinted record before the Court under stipulation, and are printed at pages xxx to xli of the appendix to this brief (R. 2341).

It should be noted at this point that these reports of the Commission, which approved and authorized the securities originally held by this respondent and the securities received in exchange therefor, and now held, contain in each case an express finding that the issue by the debtor Company of the obligations in question "is for lawful objects within its corporate purposes, and compatible with the public interest" and "necessary and appropriate for * * * the proper performance by it of service to the public as a common carrier". There will be occasion to make further reference to this fact later in this brief. (See Point II.)

The Commission had on June 9, 1930, after hearing and investigation, issued a complete and detailed report upon the applications of The Great Northern Railway Company and The Western Pacific Railroad Company for authority to construct the proposed Northern California Extension and lines connecting with the Great Northern System, and had certified

> "* * * That the present and future public convenience and necessity require the construction and operation by the Western Pacific Railroad Company of the [proposed] line of railroad * * *." (*Great Northern Railway Company Construction*, 166 I. C. C. 3, 41.)

The three notes now held by A. C. James Co. are secured by $6,249,500 principal amount of the debtor's General and Refunding Mortgage bonds, issued under its Indenture dated as of January 1, 1932, which General and

Refunding Mortgage bonds were deposited with and are now held by A. C. James Co., except that $2,000,000 principal amount of such bonds were, at the request of the debtor, delivered to The Railroad Credit Corporation, to be held by that corporation as additional collateral against advances made by it. A. C. James Co. retains all its rights as lienor in and to such $2,000,000 worth of bonds, subject only to the prior rights accruing to The Railroad Credit Corporation as a result of the delivery of such bonds, as stated above (R. 1023).

Treatment of A. C. James Co.'s secured claim under Commission Plan

In the Commission Plan, this respondent is allotted for its secured claim (principal plus interest in the aggregate amount of $6,249,750) $163,724 principal amount of Income Mortgage 4½% bonds, Series A, $256,756 of 5% Preferred Stock, Series A, and 37,635 shares of common stock of the proposed reorganized company (R. 392). Such common stock is no par value stock and in the Commission Plan it is allotted to other secured creditors at prices varying from $57 to $62 per share (R. 391-2). Using the highest price assigned by the Commission to such common stock, in allotting it to other secured creditors, the total allotment of securities to this respondent amounts to $2,753,850, against an aggregate claim of $6,249,750, or approximately 44% of the face of said claim. Using the same valuation, no other secured creditor is allotted less than 100% of its claim.

The brief for the Institutional Bondholders (p. 55) in an ingenious effort to spell out a new valuation of the debtor's properties for reorganization purposes, by assigning to the Commission's proposed capital structure a dollar total, takes the no par value common stock, which is included in the capital structure, at $57 per share. On this basis, only about 40% of this respondent's secured claim would be recognized and refunded.

Even if the common stock were to be taken at a value of $100 per share (a value used by the Commission in its reports of October 10, 1938 and June 21, 1939, in discussing capitalization,—R. 244, 245, 321) the securities allotted would fall short of a refunding of this respondent's claim, to the extent of approximately one-third.

The Commission found (R. 269) that the securities allotted to A. C. James Co., as a secured creditor, would be inadequate to satisfy its claim but did not determine or discuss the amount of the inadequacy.

The railroad system of the debtor as it exists today

For a more complete statement as to the property of the debtor and its subsidiaries and the properties operated by the debtor, the Court is referred to the printed record at pages 1037-1043.

The original line of railroad operated by the debtor ran from Oakland, California, to Salt Lake City, a distance of 924 miles.

Between 1927 and 1938 substantial additions to the railroad system of the debtor were made which have basically changed its significance as a part of our national transportation system, and have greatly increased its earning power.

The most important of these changes and additions was the construction in 1931 and 1932 of an additional line of railroad called the Northern California Extension, extending from a point on the original main line at Keddie, California, northward to connect with the Great Northern Railway Company's lines at Bieber, California. This line of railroad covers a distance of only approximately 112 miles, but because of the difficulty of the terrain through which it was built, it cost more than $10,000,000 to construct. This northward extension of the Western Pacific has opened to the debtor's railroad system en-

tirely new traffic fields and, as will hereinafter be indicated, has added greatly to the earning power of the debtor's railroad system as a whole.

In addition to the construction of the Northern California Extension, the original main line of the debtor was substantially improved and increased in efficiency by the so-called Improvement and Rehabilitation Program which was initiated in 1927 and involved the expenditure of approximately $18,000,000 between 1927 and 1938 in basic improvements of the physical property to increase operating efficiency and earning power. Of the total of $18,000,000 expended on the improvement program $8,000,000 was expended by the debtor during the period from 1927 to 1931 (R. 1052). The program was necessarily suspended at that time because of the impact of the 1929 depression. After the property was taken over by the Trustees of the Court in this proceeding, work on the program was resumed and completed during the period from 1936 to 1938 (R. 203, 1214). It was for the purpose of carrying on and completing this program that the Trustees borrowed $10,000,000 on Trustees' Certificates, to which reference will hereinafter be made in connection with the discussion of the capitalization of the debtor.

At the present time the debtor owns or operates 1,207.51 miles of standard gauge railroad (R. 1037).

One other factor of major importance should be mentioned as having a substantial effect on the economic efficiency and earning power of the debtor's railroad system. This factor was the opening in June, 1934, of the Dotsero Cut-off as part of the Denver and Rio Grande Western Railroad System. Prior to 1934 the volume of traffic received by the debtor from its important eastern connections over the Denver and Rio Grande Western Railroad Company lines, was limited, as to traffic moving to and from Chicago, by the existence of the so-called Pueblo Loop,

which so delayed traffic as to make it impossible to maintain competitive freight schedules as to freight moving between Chicago and California points. The building of the Moffatt Tunnel and the construction of the Dotsero Cut-off shortened the through route so far as Denver and Rio Grande Western movement was concerned by approximately 175 miles. This has increased and is now increasing substantially the volume of traffic received by the debtor from its important connections, the Burlington and Rock Island railroads, by way of the Denver and Rio Grande Western and the volume of traffic delivered by it to its connections, the Burlington and Rock Island railroads, by way of the Denver and Rio Grande Western (R. 215, 2099, 2100).

Investment and value of the property of the debtor

In its report of October 10, 1938, the Commission stated that the balance sheet of the debtor's Trustees as of June 30, 1938, showed total assets of $173,650,980.19 (R. 203, 1060, par. 63).

Section 19a valuation

The Commission has determined, and has stated in its report in this proceeding, the value of the property of its debtor and its wholly owned subsidiaries, pursuant to Section 19a of the Interstate Commerce Act (R. 1058-63). In its report of October 10, 1938, the Commission summarized total former valuations and concluded (R. 224):

> "* * * If there be added to the above amounts [the Commission's valuations of the properties of The Western Pacific Railroad Company and its wholly owned subsidiaries] the net cost of additions and retirements between valuation dates and December 31, 1935, the total would be $139,600,455."

The valuation of the properties of the debtor and its subsidiaries (excluding Deep Creek Railroad Company which was abandoned in 1939), as found by the Interstate Commerce Commission under Section 19a of the Interstate Commerce Act, with additions and betterments, new lines and extensions, subsequent to the dates of valuations, plus non-operating properties, (all as shown by the books of the debtor's Trustees) was in the total amount of $150,907,623.49 as of December 31, 1938 (R. 1061-2, par. 68).

Commission's prior determinations of capital assets

On February 27, 1932, the Commission, in its report authorizing the issue of $15,000,000 principal amount of General and Refunding Mortgage Gold bonds, Series A, of the debtor, found that the total capital assets of the debtor in road, equipment and affiliated companies, as of December 31, 1931 was $147,056,283.31 (R. 1060, par. 64). Again, on December 9, 1932, the Commission, in its report authorizing the issue of $4,000,000 principal amount of General and Refunding Mortgage Gold bonds, Series B, of the debtor, found the "total capital assets [to be] $148,796,047.60," as of May 31, 1932 (R. 1060, par. 65). Part of each issue of bonds was authorized to secure the notes of the debtor which were issued to A. C. James Co. in 1932 in exchange for the debentures theretofore held by it.

The Commission's valuation under Section 19a and its prior determinations of capital assets in authorizing the issue of securities to A. C. James Co. in 1932 were referred to by the Commission in its reports. But when the Commission dealt with its proposed allowable capital structure, it blandly waved aside these data, as irrelevant, under the construction which it read into Section 77 (Point II).

Secured claims against debtor and their treatment under Commission Plan

There is printed below (a) a table which shows the secured claims against the debtor, with accrued interest to January 1, 1939, the effective date used in the Commission Plan; (b) a table showing the securities which it is proposed should be issued by the reorganized company under the Commission Plan; and (c) a table showing the distribution of such proposed securities among the secured creditors. A complete list of the claims against the debtor appears at pages 1022-28 of the printed record, while the securities proposed to be authorized under the Commission Plan appear at page 364 of the record and the proposed distribution, at pages 390-2.

(a) Summary of secured claims as of January 1, 1939

Claim or Interest	Principal of claim or interest	Accrued interest at contract rate to effective date of plan	Total claim including interest at contract rate to effective date of plan
Trustees' Certificates (held by Reconstruction Finance Corporation)	$10,000,000.00	$	$10,000,000.00
Equipment obligations	2,750,050.00	94,202.00	2,844,252.00
First Mortgage 5% Bonds	49,290,100.00	13,143,776.66	62,433,876.66
Reconstruction Finance Corporation Collateral Notes (secured by General and Refunding Mortgage bonds and other collateral)	2,963,000.00	899,869.98	3,862,869.98
The Railroad Credit Corporation Collateral Notes (secured by General and Refunding Mortgage bonds and other collateral)	2,445,609.88	145,314.23	2,590,924.11
A. C. James Co. Collateral Notes (secured by General and Refunding Mortgage bonds)	4,999,800.00	1,249,950.00	6,249,750.00
Total secured Debt	$72,448,559.88	$15,533,112.87	$87,981,672.75

(b) Proposed new securities

Undisturbed equipment obligations	$ 2,750,050
New First Mortgage 4% Bonds	10,000,000
Income Mortgage 4½% Bonds	21,219,075
Five Per Cent Preferred Stock, par value $100 per share	31,850,297
Total of dollar value securities	$65,819,422
No par common stock	319,441 shares

(c) Distribution of proposed securities

(Exclusive of undisturbed equipment trust obligations and First Mortgage 4% Bonds, to be issued for new money)

Secured Creditors		Income Mortgage 4½% Bonds	5% Preferred Stock, $100 par value	No par Common Stock
First Mortgage 5% Bonds				
Principal	$49,290,100.00			
Interest to Jan. 1, 1939	13,143,766.66			
Total	$62,433,876.66	$19,716,040	$29,574,060	230,593 shares
Reconstruction Finance Corporation Collateral Notes (secured by General and Refunding Mortgage Bonds and other collateral)				
Principal	$ 2,963,000.00			
Accrued interest to Jan. 1, 1939	899,869.98			
Total	$ 3,862,869.98	1,185,200	1,777,800	15,788 shares
The Railroad Credit Corporation Collateral Notes (secured by General and Refunding Mortgage Bonds and other collateral)				
Principal	$ 2,445,609.88			
Accrued interest to Jan. 1, 1939	145,314.23			
Total	$ 2,590,924.11	154,111	241,681	35,425 shares
A. C. James Co. Collateral Notes (secured by General and Refunding Mortgage Bonds)				
Principal	$ 4,999,800.00			
Accrued interest to Jan. 1, 1939	1,249,950.00			
Total	$ 6,249,750.00	163,724	256,756	37,635 shares

Comments

With reference to the above summary statement of the situation as to the debtor's secured obligations and the provision made for them, certain points should be noted for their bearing upon the subsequent discussion in this brief.

The Trustees' Certificates of Indebtedness do not represent the refunding of any obligation of the debtor existing on August 2, 1935, when the debtor's petition under Section 77 was filed. They were originally issued in the aggregate principal amount of $10,000,000 pursuant to orders of the District Court made October 5, 1938 and November 7, 1938 (R. 1028). They were authorized by the Commission and by the District Court upon petition of the Trustees in order to provide the Trustees with the necessary funds to complete a program of rehabilitation and improvement of the debtor's railroad system, which program had been initiated in 1927 and suspended in 1930, after approximately $8,000,000 had been expended. On January 1, 1939, the effective date of the proposed Commission Plan, these Trustees' Certificates of Indebtedness were outstanding in the principal amount of $10,000,000, bearing interest at the rate of 4% and were all held by Reconstruction Finance Corporation (R. 1028). The Certificates have been renewed from time to time since January 1, 1939, and the principal amount has been somewhat reduced by amortization payments subsequently required by the Commission in connection with renewal authorizations. From their nature they constitute a first lien upon all property in the hands of the Court, and at the present time are specifically secured by $6,000,000 in cash (see p. Liii of appendix), which has been deposited from time to time with the Reconstruction Finance Corporation by the Trustees pursuant to an order of the District Court, dated November 26, 1941.

The collateral notes held by Reconstruction Finance Corporation, as shown in the above tables, are an obligation of the debtor in the principal amount of $2,963,000, secured by $10,750,000 principal amount of the debtor's General and Refunding Mortgage bonds and also by additional collateral pledged by parties other than the debtor (R. 1023-4).

The secured notes held by The Railroad Credit Corporation in the principal amount of $2,445,609.88 are secured by $4,000,000 principal amount of the debtor's General and Refunding Mortgage bonds and by other collateral, including a subordinate lien upon all collateral pledged by the debtor with the Reconstruction Finance Corporation (R. 1024-5). The General and Refunding Mortgage bonds held by The Railroad Credit Corporation include $2,000,000 principal amount, which were originally deposited with and held by the A. C. James Co. A. C. James Co. retains all its rights as lienor in and to such $2,000,000 worth of bonds, subject only to the prior rights accruing to The Railroad Credit Corporation as a result of the delivery of such bonds, as stated above (R. 1023).

In addition to the secured claims shown by the above tables, the debtor owed to Western Pacific Railroad Corporation and The Western Realty Company $5,818,791 principal indebtedness upon open account which, with interest at the contract rate to the effective date of the plan, amounted to a total unsecured debt of $7,810,887 (R. 1026-7).

Further, the tables set out above do not show the stock of the debtor, all of which is held by Western Pacific Railroad Corporation, being $28,300,000 par value of preferred stock and $47,500,000 par value of common stock (R. 1027).

Revenue and earnings

In the report of the Commission of October 10, 1938, there appears a somewhat extended discussion of the past earnings history of the debtor's system and there is subsequent discussion of this earnings record in the Commission's later report of June 21, 1939 (R. 218, 308).

This discussion of earnings in the Commission's reports is of little value because of the almost complete failure to distinguish between the earnings of the property of the debtor as that system existed prior to the changes made from 1927 to 1938, and the earning power of the debtor's railroad system as it now exists after the substantial changes made between 1927 and 1938, including (a) the construction and operation of the Northern California Extension; (b) the completion in 1938 of the Improvement and Rehabilitation Program; and (c) the beneficial effects of the building of the Dotsero Cut-off on the amount of traffic received from and delivered to the Burlington and Rock Island railroads by way of the Denver and Rio Grande Western.

The entire discussion by the Commission in its reports of the earnings history of the debtor is further colored by its misconception of its task under Section 77 of the Bankruptcy Act. As will be pointed out later in this brief, the Commission has assumed under purported authority of Section 77 to deal with property rights of secured creditors and other parties in interest on the basis of the supposed necessity of limiting total capitalization solely in the public interest. It has, therefore, not concerned itself primarily with the basic question of "earning power" which it would necessarily have faced if it had felt constrained to revalue the existing properties of the debtor under subsection (e) of Section 77 of the Bankruptcy Act, where "earning power" as distinct from "earnings" and "probable earnings" is expressly made the primary determinative factor.

When the Commission Plan came before the District Court, the parties to the proceeding entered into a stipulation for the convenience of the Court, which included a statement of the railroad operating revenues of the debtor's system from 1922 (the end of Federal control) to the latest available date (R. 1064), and a statement of adjusted consolidated earnings available for interest (R. 1065-6) for the same period.

The earnings data shown in the stipulation of the parties, referred to above, has been supplemented as to the subsequent periods by monthly statements prepared by the Trustees in charge of the operation of the debtor's property and filed with the Clerk of the United States District Court for the Northern District of California, Southern Division, and duly certified to the Circuit Court of Appeals for the Ninth Circuit pursuant to order of the District Court (R. 2627). These statements appear for the period from December, 1939 to September 1941, in Volumes VII and VIII of the printed record. Subsequent statements covering the periods since September, 1941, have been submitted to this Court and are a part of the unprinted record available, under stipulation of the parties filed with this Court, for use in brief or in argument. For the convenience of the Court these statements for the months, December, 1940 (which includes operating results for the calendar year 1940), December, 1941 (which includes operating results for the calendar year 1941), June, 1942 (which includes operating results for the first six months of 1942) and July, 1942 are printed in the appendix of this brief at pages L to Liii.

The two tables set forth below show in summary form (a) railway operating revenues of the debtor's system and (b) adjusted consolidated earnings available for interest:

(a)

Railway Operating Revenues of the Debtor's System

Year	Freight	Passenger	Other	Total
1922	$ 9,667,960	$2,184,093	$ 884,511	$12,736,564
1923	10,751,276	2,455,420	1,208,116	14,414,812
1924	11,241,579	2,106,656	1,321,078	14,669,313
1925	12,634,074	2,000,817	1,263,657	15,898,548
1926	14,259,651	2,319,151	1,372,666	17,951,468
1927	14,764,690	2,090,480	1,451,505	18,306,675
1928	15,974,137	1,870,790	1,576,924	19,421,851
1929	16,358,041	2,187,700	1,550,816	20,096,557
1930	15,450,051	1,795,834	1,573,177	18,819,062
1931	12,342,041	1,315,283	1,195,614	14,852,938
1932	10,662,430	764,977	823,664	12,251,071
1933	10,950,948	595,268	656,273	12,202,489
1934	12,338,085	629,720	811,433	13,779,238
1935	13,254,572	730,957	421,929	14,407,458
1936	15,264,675	805,673	476,996	16,547,344
1937	16,588,843	814,632	515,010	17,918,485
1938	14,934,497	680,382	442,572	16,057,451
1939	16,819,157	1,014,887	473,477	18,307,521
1940	18,701,678	860,047	436,617	19,998,342
1941	24,119,568	873,174	553,741	25,546,483

1942: Total for first six months, $16,235,602 (representing an increase of $6,124,602 or 60.57% over the corresponding total for first six months of 1941).

(b)

Adjusted Consolidated Earnings Available For Interest

1922	$2,040,890
1923	4,412,234
1924	3,241,823
1925	4,557,798
1926	4,868,390
1927	3,470,861
1928	4,376,972
1929	3,718,436
1930	2,381,529
1931	220,494 (deficit)
1932	283,912
1933	474,365
1934	1,396,353
1935	1,377,026
1936	1,901,423
1937	1,077,407
1938	225,431
1939	1,519,916
1940	2,649,797
1941	4,548,138

1942: First six months, $4,080,090 (representing an increase of $2,996,563, or 276.56% over the corresponding period of 1941).

Earning Power of the Property

The discussion of earnings in the briefs of the petitioners is essentially misleading in several respects.

In the first place, they find it necessary to deduct from the actual earnings available for interest in recent years substantial sums of theoretical Federal taxes, not actually paid or payable, on the theory that *if* the Commission Plan had been in effect, it would have converted 60% of the First Mortgage debt into equity holdings and so would

result in moneys that would be deductible from income as interest, under the old capital structure, becoming subject to tax as equity earnings under the Commission Plan.

In the second place, the petitioners give only lip service (see note, p. 7 and p. 14, Institutional Bondholders' brief) to the substantial changes which occurred in the debtor's railroad system between 1927 and 1938, inclusive, and completely fail to give due weight to the fact that the railroad system of the debtor, as it has existed since 1938, is a substantially different property from the original railroad system as it existed during the prior years of the period which they discuss.

It may fairly be said, however, as to the property to be reorganized, that no amount of parading of historical earnings, no matter how skillful, can disguise the fact that in the calendar year 1941 the debtor's railroad system earned by a wide margin its interest requirements under its existing capitalization (prior to the drastic and unsupported changes proposed in the Commission Plan). In other words, during the calendar year 1941, after the debtor's railroad system had earned all interest requirements on its equipment obligations, the Trustees' Certificates, its outstanding First Mortgage bonds and its secured debts (including the claim of this respondent) there were left excess earnings of approximately $1,218,000.

Further, no amount of skillful argument or chart-making can cloud or conceal the fact that during the twelve month period from August 1, 1941 to July 31, 1942, as shown by the earnings statements filed by the Trustees in this proceeding pursuant to order of the District Court and before this Court, by stipulation, the debtor's railroad system earned $7,987,512 available for interest, a sum sufficient to cover its old fixed charges more than twice.

Obviously the current earnings of the debtor's railroad system, as it exists today, constitute a fair return on the

fully depreciated investment of the debtor in property used in the service of the public, as disclosed by the record in this proceeding (R. 1063, 283, 357).

If "earning power" is to be construed, as this respondent contends it should be, as "*capacity* to produce earnings," then it must be conceded that the Section 19a valuation of the properties of the debtor of approximately $150,000,000 as previously found by the Commission and reported in this proceeding, cannot fairly or soundly be whittled down or reduced on the basis of lack of "capacity to earn," under any reasonable construction of the valuation provisions of subsection (e) of Section 77. And it must equally be conceded that any reasonable valuation, giving full weight to demonstrated earning power, would exceed by a substantial margin the amount required to make provision for all of the debtor's secured debts, including the claim of this respondent.

Nor can it soundly be urged that these increased recent earnings are solely, or even in principal part, due to war conditions. It is, of course, admitted that the gross and net earnings of all railroad carriers, and especially of those vital carriers which are essential links in our transcontinental movement to the Pacific coast, have been increased by the pressure of war transportation.

In the case of the debtor's railroad system, however, other and vital factors exist which necessarily tend to raise the level of earnings substantially above the level which would have existed for the original property. These factors include, as pointed out above, (a) the construction and operation of the Northern California Extension; (b) the completion in 1938 of the Improvement and Rehabilitation Program; and (c) the substantial, though indirect, benefits of increase in traffic volume due to the functioning of the Dotsero Cut-off on the Denver & Rio Grande Western Railroad System. As to "b" and "c", it is diffi-

cult to establish, from the record before this Court, any measure of the extent of improvement in gross and net earnings which may be attributed to those factors. As to the Northern California Extension, however, there is available data in the record which permits some rough measurement of the substantial change in the earning power of the debtor's railroad system, which flowed from the construction and operation of this line of railroad.

Increase in Earning Power Due to Northern California Extension

The Northern California Extension was built in 1931 and 1932 and was opened to traffic in the latter year. There was, of course, a necessary lag in the full utilization of this line of track as an income producer during a seasoning period, which may fairly be deemed to have extended from 1932 to 1936. During that period traffic exchange arrangements were being worked out with other carriers, and other carriers and shippers were being educated to the use of the alternative routings of traffic made possible by the construction of this line. The fact that the Commission had authorized the construction of this line because the "public convenience and necessity" required it, did not mean that its full economic usefulness would be immediately evident to other carriers and to shippers. A period of education and seasoning was necessary.

In the stipulation submitted by the parties to the District Court the increase in gross traffic attributable to the Northern California Extension is set forth (R. 1078). Complete data are available only for the years 1932 to 1938, inclusive. The following table has been prepared to show the relation of revenues attributable to the Northern California Extension to other revenues of the property:

CONSOLIDATED GROSS REVENUES FROM FREIGHT

Year	Originated and terminated on and passing over Northern California Extension	Other	Total	Ratio of Northern California Extension revenue to other revenue
	(1)	(2)	(3)	(4)
1932	$1,098,016	$ 9,564,414	$10,662,430	11.48%
1933	1,491,466	9,459,482	10,950,948	15.77%
1934	2,119,427	10,218,658	12,338,085	20.74%
1935	2,289,858	10,964,714	13,254,572	20.88%
1936	3,151,734	12,112,941	15,264,675	26.02%
1937	3,425,601	13,163,242	16,588,843	26.02%
1938	3,093,674	11,840,823	14,934,497	26.13%
1939 (9 mos.)	2,463,489	9,221,006	11,684,495	26.72%

(1) Record, p. 1078.
(2) Derived; (3)—(1).
(3) Record, p. 1064.
(4) Derived; (1)÷(2).

It will be noted that beginning with 1936, after the Northern California Extension became seasoned as an artery of traffic, it increased, for the period covered, the gross revenue from the debtor's other lines by approximately 26%. While the record before the Court does not include the necessary data for completion of the table to date, the facts are known to all parties to the proceeding and shown by the records kept by the Trustees appointed by the District Court, who are operating the property, and it may be stated without fear of contradiction that this ratio of a 26% contribution of the Northern California Extension has been maintained with substantial consistency in the years subsequent to the period covered by the table above.

If one were to project back to the pre-depression years a 26% contribution to gross from a part of the debtor's system which did not then exist, a quite different historical earnings' picture would be presented. This is especially so when one takes into account that a much larger part of this additional gross would necessarily be carried to earnings available for interest, owing to the more economical use of motive power and the better balancing of the flow of traffic which has been made possible by the new sources of traffic coming from the Northern California Extension.

Obviously it is the debtor's railroad system, as it exists today, and not as it existed in the pre-depression years, which is to be reorganized. It is the "earning power" of the debtor's present railroad system and not the earning power of the system as it existed prior to 1938 that must be given consideration.

While it is not possible to measure as definitely the effects of the other factors mentioned (Improvement and Rehabilitation Program and the Dotsero Cut-off), as one can the effect of the Northern California Extension, this Court cannot properly close its eyes to the fact that the present railroad system of the debtor is quite a different railroad system from that whose earnings are largely discussed by the Commission and by the petitioners.

Significance of earnings history in relation to authorization and treatment of this respondent's secured claim

By way of further comment on the earnings statements set out above, attention should be called to the significance of these earnings statements with reference to the secured claim of this respondent and its proposed treatment in the Commission Plan.

The securities which the A. C. James Co. holds were authorized by the Commission in 1932 as "compatible with

the public interest" (pp. 11, 12, above). In 1938 and 1939 the Commission (ostensibly proceeding on the same theory as to public interest in capitalization as in 1932) by its Plan asserted the proposition that with reference to the earnings of debtor, the securities held by the A. C. James Co. could no longer continue to remain in existence, except as to 44% of the amount authorized in 1932 when this respondent purchased those securities for cash at their full face value. And yet, if the Court will look at the adjusted consolidated earnings available for interest, as set out above (p. 24), it will note that the average earnings of the debtor for the three-year period from 1930 to 1932 were $814,982. Comparing that period with the three-year period from 1937 to 1939, inclusive, the average earnings for the latter period were $941,752 and so in excess of the earnings for the three-year period prior to the authorization by the Commission "as compatible with the public interest" of the securities held by the A. C. James Co.

If the "earning power" of the debtor supported the creation, "in the public interest" of this respondent's secured claim in 1932, the "earning power" of the debtor supported the full recognition and refunding of that claim in 1939, and did not give a basis for the foreclosure and cancellation of more than half of the claim. Any such doctrine of foreclosure and cancellation as is here asserted by the Commission, if sustained under these circumstances, would be an overwhelming deterrent to any fufure participation by private investors in the transportation field.

Some reference will hereafter be made to this phase of the earnings history of the debtor in the discussion of the attempt of the petitioners to justify the theory upon which the Commission has proceeded in foreclosing the interest of creditors, by reference to an alleged continuity of functioning by the Commission under Section 20a of the Interstate Commerce Act (as it was functioning when it authorized the securities acquired by the A. C. James

Co. in 1931 and 1932) and its functioning under Section 77 of the Bankruptcy Act, under which it claims to exercise a legislative grant of power to foreclose the rights of the A. C. James Co. as a secured creditor.

Further required adjustments in past earnings record

While the table of earnings, which appears on page 24 above, is designated as a table of "adjusted consolidated earnings available for interest" it should also be remembered that the adjustments consisted in mere accounting corrections which took out of the operating expenses, expenditures in connection with the Improvement and Rehabilitation Program, which had, under Commission rules, been charged in part as operating expenses. There is, of course, no attempt to make any adjustment for the necessarily high level of operating expense which arose from the characteristics of the operating property and made it necessary that there be spent during the period from 1927 to 1938 $18,000,000 in the Improvement and Rehabilitation Program. The operating expenses of the period prior to 1938 were necessarily higher than they are currently, or will be in the future, now that the program has been completed.

It is also obvious that the continued necessity during the period from 1927 to 1938 to carry on construction work at various points on the property in connection with the Improvement and Rehabilitation Program and the construction of the Northern California Extension, involved delays and interference with normal traffic movements during the period, which resulted in substantially increased transportation costs.

Nor do the adjustments proposed take into account the known fact, of which the Court may properly take judicial notice, that the railroads, generally, during the depression years, made enormous progress in the efficiency

of operation, which permits them to retain a larger proportion of gross as net, despite increases in labor cost.

It is also of some interest to note that the original railroad system of the debtor, before the construction of the Northern California Extension, before the completion of the Improvement and Rehabilitation Program and before the opening of the Dotsero Cut-off on the Denver and Rio Grande Western, showed earnings for the eight-year pre-depression period, from 1922 to 1929, inclusive, considerably in excess of the earnings which the Commission apparently anticipated in its reports of October 10, 1938 and June 21, 1939, from the property as it is today with its greatly increased earning power. In the years 1922 to 1929 the old main line property showed earnings available for interest averaging $3,878,426 per year (R. 1065). If one were to give effect only to the increase of earnings which would be reasonably attributable to the increased gross from the Northern California Extension, one might fairly say that the average earnings available for interest for that period would have been increased by at least 26% and bring the earnings for the period to approximately $5,000,000 per annum.

This, however, is not the only necessary adjustment upwards of historical earnings because the other changes in earning power of the present property, as compared with the old property, to which reference has been made, cannot fairly be disregarded.

Summary of Argument

This respondent contends that no plan of reorganization under Section 77 of the Bankruptcy Act can be fair and equitable, which forecloses more than half of the claim of a secured creditor except on the basis of a clear showing and definite findings or determinations that the value of the property of the debtor is less than the amount of the secured claims with accrued interest.

The Commission has found specifically (R. 269) that under its Plan the claim of this respondent is not fully recognized or refunded. The Commission reports (R. 224) its Section 19a valuation of the debtor's railroad system as of December 31, 1935, as approximately $139,000,000. With additions and betterments to the effective date of the Commission Plan, this Section 19a valuation amounts to approximately $150,000,000 (R. 1061-2). This is an amount far in excess of that needed to permit full recognition and refunding of respondent's secured claim. The Commission has made no finding or determination that this previously found value of $150,000,000 should be reduced to some other and lesser amount based on lack of "earning power," nor has it even made a specific finding or determination as to the "earning power" of the debtor as a required element for consideration in determining the value of the properties of the debtor under subsection (e) of Section 77 of the Bankruptcy Act.

This respondent contends that the Commission erred in formulating and certifying its plan of reorganization and that the District Court clearly erred in approving such plan. It maintains that the Circuit Court of Appeals acted properly in reversing the judgment of the District Court and should be affirmed.

This respondent further contends that the errors into which the Commission and the District Court fell were due to basic errors in their construction of the legislative mandate imposed by Section 77 of the Bankruptcy Act, and urges this Court that it hand down, for the benefit of the Commission and of the inferior courts, a definitive and final interpretation of Section 77, as applicable to the facts herein involved, in order that the reorganization of the debtor railroad may be effectuated expeditiously and without substantial injustice to this respondent and other interested parties.

The argument of this respondent in support of its basic contentions is set forth in the following points:

Point I

The findings and determinations of the Commission and the District Court as to essential facts are obviously insufficient to justify or support the treatment of respondent's secured claim, which treatment is clearly confiscatory.

Point II

The Commission's construction of Section 77 of the Bankruptcy Act, which was accepted and adopted by the District Court, is basically erroneous and cannot be sustained either under the language or intent of Section 77 of the Bankruptcy Act or under any prior delegation of authority to the Commission in connection with the issue of securities by railroads.

Point III

The Commission's assumption of a legislative mandate under Section 77 authorizing it to convert valid debt into stock finds no support in the language of Section 77 and carries with it practical consequences seriously prejudicial to the credit of the debtor.

Point IV

Section 77 of the Bankruptcy Act does not delegate to the Commission authority to originate and impose upon the parties a plan of reorganization and to nullify completely the rights of the parties to propose and negotiate a fair and equitable plan.

Point V

The groups of security holders represented in this proceeding should be permitted, under supervision by the Commission and the courts as contemplated by Section 77, to renegotiate their contractual relationships, and formulate and agree upon a plan of reorganization, which would (a) observe the rule of

priorities of the *Boyd* and *du Bois* cases, (b) provide for fixed charges only to the extent that they shall be adequately covered by "probable earnings", and (c) provide for a total capitalization within the limit established by the value of the property of the debtor used in the public service, after due consideration of its earning power.

POINT VI

The District Court in this case failed to exercise an informed and independent judgment in approving the Commission Plan.

POINT VII

Preferential treatment given the claim of the Reconstruction Finance Corporation under the Commission Plan is unsupported by necessary administrative or judicial findings and cannot be justified under the facts of this case.

POINT VIII

The General and Refunding Mortgage is a first lien upon assets of the debtor sufficient in value to cover fully the claims of the three secured creditors, including this respondent.

POINT I

The findings and determinations of the Commission and the District Court as to essential facts are obviously insufficient to justify or support the treatment of respondent's secured claim, which treatment is clearly confiscatory.

The claim of this respondent was classified by the District Court as a separate class of claim by its order of August 20, 1935 (R. 1022-3). The Commission itself has expressly found that the securities proposed to be given to this respondent under the Commission Plan will be inadequate to satisfy its claim (R. 269, 317).

Nowhere in the report of the Commission of October 10, 1938, or in its report of June 21, 1939, can there be found any valuation of the property of the debtor, other than the Commission's valuation under Section 19a of the Interstate Commerce Act, which it expressly finds in its report of October 10, 1938, to have been $139,600,455 as of December 31, 1935 (R. 224) and which, with additions and betterments to the effective date of the Commission Plan, amounted to approximately $150,000,000 (R. 1061-2).

This Section 19a valuation, as determined and reported by the Commission was, of course, largely in excess of the total of secured claims, principal and interest, which as shown above (p. 17) amounted, as of January 1, 1939, to only $87,981,672.75.

It is of some significance also in this connection to refer to the fact that the original cost of the properties of the debtor, less full depreciation amounted to upwards of $120,000,000. This figure is net, after full accrued depreciation not only on equipment but also on ways and structures which latter, in accordance with Commission accounting rules, does not appear in the debtor's property accounts as an accrued item, as shown by the record and as stated by Commissioner Miller in his opinion in connection with the report of the Commission of October 10, 1938 (R. 283, 357, 1063).

The Commission rejected three plans submitted by the parties to this proceeding, each of which proposed a limit of capitalization well within the Commission's 19a valuation and well within the fully depreciated investment of the debtor in its railroad system, and each of which contemplated refunding the claim of this respondent in full. The Commission, in its Plan, confiscates and refuses to refund more than half of this respondent's secured claim, yet deliberately refrains from making any modified valuation of the debtor's property under subsection (e) of Section 77 of the Bankruptcy Act.

This Court has had occasion in the recent past to reiterate and emphasize the established doctrines of law which support the contention of this respondent, that the property interest of a secured creditor cannot lawfully be foreclosed and confiscated under the bankruptcy powers except on the basis of a valuation of the assets of the debtor which would support such treatment.

In dealing with a somewhat analogous statute (Section 77B, now Chapter X of the Bankruptcy Act), this Court held squarely in *Consolidated Rock Products Co.* v. *du Bois*, 312 U. S. 510, that a valuation of the assets of the debtor was a condition precedent to any determination by the Court as to the fairness of a plan of reorganization.

It should be noted that in the *du Bois* case there was an agreement of a large majority of each class of creditor and stockholder upon a plan of reorganization. That is a situation which does not exist in the instant case, where the Commission has rejected all plans submitted by the parties and seeks to impose upon the parties a plan of its own formulation which is supported in this Court by only two classes of creditors.

In the *du Bois* case, *supra*, the District Court had approved the proposed plan of recapitalization for the reorganized company without ascertaining either the value of the property as a whole or the value of the assets securing the respective claims. This Court held that the interests of a secured creditor, a small minority of his class, could not be foreclosed without determination of the value of the property of the debtor and the assets subject to secured claims and appropriate findings as to earning power. As to the need of adequate valuation data, the Court said, at page 520:

> "We agree with the Circuit Court of Appeals that it was error to confirm this plan of reorganization.

"I. On this record no determination of the fairness of any plan of reorganization could be made. Absent the requisite valuation data, the court was in no position to exercise the 'informed, independent judgment' (*National Surety Co.* v. *Coriell*, 289 U. S. 426, 436) which appraisal of the fairness of a plan of reorganization entails. *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106. And see *First National Bank* v. *Flershem*, 290 U. S. 504, 525. There are two aspects of that valuation problem.

"In the first place, there must be a determination of what assets are subject to the payment of the respective claims. This obvious requirement was not met. The status of the Union and Consumers bondholders emphasizes its necessity and importance. According to the District Court the mortgaged assets are insufficient to pay the mortgage debt. There is no finding, however, as to the extent of the deficiency or the amount of unmortgaged assets and their value. * * *"

Again, at page 525:

"* * * Findings as to the earning capacity of an enterprise are essential to a determination of the feasibility as well as the fairness of a plan of reorganization. * * *"

In dealing with the rights of secured creditors in the *du Bois* case, this Court merely enunciated well established and well defined principles as to fairness and equity in dealing with the rights of secured creditors. It did not have before it there, as it does here, a statute which contained express provision for the making of valuations by an administrative agency such as are contained in subsection (e) of Section 77 of the Bankruptcy Act. The principles which this Court has laid down in the *du Bois* case should, therefore, be applied with full and undiminished force to the situation presented by the confiscatory treatment of the secured claim of this respondent on the basis of a record which contains no findings of any valuation which would support such treatment.

There can be no advantage in referring to decisions of this Court, other than those cited in the *du Bois* case, which support by analogy the clear cut principle laid down in that decision. It is, however, of some importance to emphasize at this point the attitude which this Court has previously taken as to any attempt to foreclose substantial rights of a secured creditor in the operation of the Bankruptcy Act.

In *Louisville Joint Stock Land Bank* v. *Radford*, 295 U. S. 555, this Court held the first Frazier-Lemke Act unconstitutional. In rejecting the argument that the statute was valid by analogy to the validity of compositions under the Bankruptcy Act, the Court said (pp. 585-6):

> "* * * In no case of composition is a secured claim affected except when the holder is a member of a class; and then only when the composition is desired by the requisite majority and is approved by the court. Never, so far as appears, has any composition affected a secured claim held by a single creditor. * * *"

At pages 588-9:

> "It is true that the position of a secured creditor, who has rights in specific property, differs fundamentally from that of an unsecured creditor, who has none; and that the Frazier-Lemke Act is the first instance of an attempt, by a bankruptcy act, to abridge, solely in the interest of the mortgagor, a substantive right of the mortgagee in specific property held as security. * * *"

Nowhere in the reports of the Commission or in the opinion of the District Court, can be found a determination or finding as to the value of the properties of the debtor on which the treatment of this respondent's secured claim could properly be held to be not confiscatory. The Commission's valuation under Section 19a of the Interstate Commerce Act (R. 224) was far in excess of the total of all secured claims.

The Commission's discussion and general conclusions (R. 220, 245, 253) as to the debtor's revenues and earnings, its limitation upon total capitalization which includes no par common stock (R. 310, 341), its conclusion that "the securities remaining available for distribution * * * to the other secured creditors [including A. C. James Co.] * * *, will be inadequate in value to satisfy their claims" (R. 269, 271) are wholly inadequate as substitutes for the determinations of value required by this Court (*du Bois* case, *supra*).

The blanket adoption of the Commission's "findings" by the District Court and its approval of the plan in the language of the statute, cannot clarify or remedy the obscurity and inadequacy of the Commission's conclusions.

This Court should not be required "to spell out, to argue, to choose between conflicting inferences" from obscure phrases and suggestions in the Commission's report (*United States* v. *Chicago, Milwaukee, St. Paul & Pacific R. Co.*, 294 U. S. 499, 511; cf. *N. L. R. B.* v. *Virginia Electric and Power Co.*, 314 U. S. 469). The lack of essential findings cannot be supplied by general conclusions in the language of the statute (*Florida* v. *United States*, 282 U. S. 194, 213, 215).

Nor can the supposed doctrine of "equitable equivalent", advanced by the petitioners as an eleventh hour substitute for the determinations of value and earning power which are required by the decision of this Court in the *du Bois* case, *supra*, relieve the Commission and the District Court of the duty of making necessary findings. The phrase itself "equitable equivalent" is taken by the petitioners from the report of the Commission (R. 316) where the Commission said (speaking of the securities approved in its Plan):

> "* * * These securities represent the equitable equivalent of the debtor's assets available for the satisfaction of claims. * * *"

This language can mean only that the securities to be issued in the reorganization represent the assets of the debtor which are available for the satisfaction of all claims. It assumes an answer to the very question in issue,—the total value of the property represented by the securities to be issued in the reorganization. It does not and cannot tell us why more securities may not be authorized, or why less securities are not authorized,—questions which must be answered from a consideration of earning power and values. The all-concealing phrase "equitable equivalent" does not tell us why the claims of some creditors are not to be recognized at all or why A. C. James Co. is to receive only 44% of its secured claim, while the "equitable equivalent" for First Mortgage bondholders and Reconstruction Finance Corporation is full compensation for their respective "bundles of rights."

In the hands of the petitioners the Commission's casual phrase is expanded and translated into a doctrine that each creditor is entitled to receive only its "equitable equivalent of the debtor's assets available for the satisfaction" of its claim in new securities (Institutional Bondholders' brief, p. 79). From this premise, which apparently represents an attempt to alter by restatement the doctrine of the *Boyd*[1] and *du Bois* cases, petitioners would conclude that valuation data and determinations of all relevant facts as to liens are unnecessary and that each secured creditor has received its "equitable equivalent" under the Commission Plan. But after this juggling of phrases A. C. James Co. is told that more than half of its secured claim must be refused recognition and confiscated because (for undisclosed reasons) its claim is not entitled to receive an "equitable equivalent."

The requirement of Section 77(d) that "the Commission shall state fully the reasons for its conclusions" certainly is not satisfied by the use of a phrase which is designed

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[1] *Northern Pacific Ry.* v. *Boyd*, 228 U. S. 482.

to conceal rather than to reveal reasons for conclusions. A secured creditor, we submit, is entitled to reasons in the form of facts and findings rather than evasion. The absence of findings or determinations as to the value of the debtor's property and as to the value of the assets securing respondent's claim constitutes, without more, a basic and fatal defect in procedural due process in view of the attempt under the Commission Plan, to wipe out more than half of respondent's claim.

While, as suggested above, a detailed reply to some of the ingenious arguments advanced by the petitioners in support of the action by the Commission and the District Court will be presented in a reply brief, which will be filed on behalf of this respondent prior to the date of the argument, there is one contention advanced in the Institutional Bondholders' brief (pp. 76-77) which should be discussed at this point.

This contention is that it requires only the mathematical process of adding the par value securities to the sum obtained by multiplying the no par value common stock authorized under the Commission Plan by $57 a share to arrive at what the brief terms a "*maximum* 'reorganization value'" in the amount of $84,027,559. Apparently, the argument is that the action of the Commission in fixing the capitalization should be regarded as what might fairly be termed the "equitable equivalent" of a finding of "reorganization value", or "a precise dollars and cents value", to be spelled out by mathematical process from the Commission's careful avoidance of specific findings.

On page 77 of the Institutional Bondholders' brief the argument continues with the following statement:

> "The complete lack of realism in the decision of the Court below upon this point is evidenced by what the Commission has tried to do to bring its more recent reports and orders into **colorable compliance** with that decision. In those cases the Commission,

after making exactly the same type of findings with respect to earning power and permitted capitalization that were made in the *Western Pacific* case, has added a final finding of which that in the *Denver & Rio Grande Western* case is typical:

> 'Considering the entire record, and taking into account the elements of value of the properties involved, their past and present earnings and prospects for future earnings, as well as other pertinent factors, we conclude and find *that the value of the properties for the purposes of this proceeding* is $154,521,612, and that the total capitalization upon consummation of the plan should not exceed approximately that amount.'

"It is submitted that the addition of the italicized words, which are not to be found in *haec verbes* in the Commission's *Western Pacific* Report, would add absolutely nothing of substance for the information either of the court or of the securityholders beyond what the Commission provided in the findings summarized at pages 14 to 18, *supra*, and the voluminous 'valuation data' discussed by the Commission in 'stating fully the reasons for its conclusions.'"

The argument that it would be a futile thing for this Court to affirm the requirement of the Circuit Court of Appeals that a finding of value should be made because the Commission could make a *pro forma* compliance without disturbing its plan loses considerable force in the light of the relative facts.

The Commission, in compliance with the requirement of the *du Bois* case and of the decision of the Circuit Court of Appeals for the Ninth Circuit in this proceeding, did find in Finance Docket No. 11002 a value of the assets of the Denver & Rio Grande Western, as debtor, in the amount of $154,521,612. In the same report (p. 9, mimeo.) the Commission stated that its prior Section 19a valuation of the properties of the Denver & Rio Grande Western System, fully depreciated to January 1, 1941, amounted to approximately $155,900,000. **In other words, there was**

a discrepancy between the Commission's prior valuation of physical properties found under Section 19a and its valuation for the purpose of reorganization of less than one per cent.

If, however, the Commission should attempt to bolster the plan which it has formulated and promulgated for the Western Pacific by any finding of value in the amount of $84,027,559, as suggested by the Institutional Bondholders' brief upon the basis of their mathematical computation of what the proposed capitalization may have meant, the Commission would need in common fairness to give some detailed and specific explanation of a discrepancy between its prior Section 19a valuation of approximately $150,000,000 (pp. 15-16, above) and a valuation for the purpose of reorganization of $84,027,559.

The difficulties of any such explanation would be accentuated by the fact that the Western Pacific Railroad System, as shown by the record before the Court in this proceeding, is a completely rehabilitated, modernized and effective transportation system, while the Court may well take judicial notice of the fact that the properties of the Denver & Rio Grande Western include a substantial mileage of narrow gauge railroad built originally to serve limited industrial areas and the well-known Pueblo Loop, the earning power of which has been largely reduced by the construction of the Dotsero Cut-off.

This further comment may fairly be made: this respondent earnestly and adversely criticizes in this brief the construction which the Commission, unaided by prior judicial construction, has given to Section 77; this respondent cannot, however, accept without protest any suggestion, such as is made in the Institutional Bondholders' brief, that the Commission has, or would, attempt a mere "colorable compliance" with a binding judicial interpretation of Section 77. The long and honorable record of the Commission as an administrative agency forbids any such implication of bad faith.

POINT II

The Commission's construction of Section 77 of the Bankruptcy Act, which was accepted and adopted by the District Court, is basically erroneous and cannot be sustained either under the language or intent of Section 77 of the Bankruptcy Act or under any prior delegation of authority to the Commission in connection with the issue of securities by railroads.

When Congress enacted Section 77 of the Bankruptcy Act, it was fully aware that the Commission, functioning under authority of Section 19a of the Interstate Commerce Act (49 U. S. C. A. §19a) had completed, at great expense to the public as well as to the carriers, valuations of the properties used by the various railroads in the service of the public. Congress further knew that these valuations were kept up to date by the Commission through its accounting supervision of additions and betterments. Congress knew that the Commission was in a position to approve or disapprove any capital structure submitted to it in a plan of reorganization under Section 77, with full and complete knowledge already available to it of the value of the capitalizable assets which would support the proposed capital structure.

By its 1935 amendment to Section 77 Congress went further. It provided that if it should be necessary to determine the value of any property for any purpose under the Section, that such valuation should give due consideration to "earning power." The legislative intention, which is discussed more fully later in this brief, seems entirely clear. Congress did not direct the Commission to disregard its extended and expensive labors in arriving at the true investment in and value of railroad properties. It merely gave the Commission power, for the purposes of Section 77, to modify such values in the light of any basic changes in earning power.

Provisions of the Statute

Section 77(e) contains the following provision requiring a valuation of the debtor's properties if a valuation shall be necessary for any purpose (appendix, p. xvii):

> "If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

Section 77(b) also requires that the plan of reorganization

> "* * * (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; * * *."

It should be noted that this provision speaks of "probable prospective earnings" while the valuation paragraph of subsection (e) speaks of "earning power." The importance of this difference in phrasing will be more fully discussed in Point V of this brief, dealing with the construction of Section 77 of the Bankruptcy Act which this respondent urges upon this Court.

Commission's Theory of Capitalization in Lieu of Valuation

The Commission, however, has deliberately refused in this proceeding to make a modified valuation of the properties of the debtor based on actual "earning power".

Instead, the Commission has adopted a gloss on Section 77, which finds no support in the language of the Section, which it regards as justifying its confiscatory treatment of private rights without reference to the value of the assets of the debtor.

The entire theory and approach of the Commission, as applied in this reorganization proceeding, is not only without support under the language of the statute, but is also without practical justification. The Commission seeks to cure the depression ills of the railroad industry by disregarding and confiscating the property interests of investors, used and useful in the public interest. Reducing capitalization below the actual depreciated investment on the basis of depression earnings is the twin brother of the write-up of investment, in terms of capitalization, which occurred in the public utility field in the golden era of 1920 to 1929, on the basis of expanded earnings of that period. That practice now receives universal condemnation. The theory of the Commission, as set out in its reports in this case, is equally unsound and should equally be condemned.

The Commission's theory and construction of Section 77 disregard a basic feature characterizing private investment in the transportation field. The public is entitled to have available a transportation plant which will meet not merely its needs during subnormal periods, nor even its needs during normal periods, but a transportation plant capable of handling the peak traffic of periods of industrial expansion. The Court has given expression to this

basic characteristic of property devoted to a public use in analogous situations. Reference is here made to the decision of the Court in *New York & Queens Gas Co.* v. *McCall*, 245 U. S. 345, where, at page 351, the Court said:

> "Corporations which devote their property to a public use may not pick and choose, serving only the portions of the territory covered by their franchises which it is presently profitable for them to serve and restricting the development of the remaining portions by leaving their inhabitants in discomfort without the service which they alone can render. To correct this disposition to serve where it is profitable and to neglect where it is not, is one of the important purposes for which these administrative commissions, with large powers, were called into existence, * * *."

There is a necessary corollary of the proposition that the public is entitled to a transportation plant which will meet maximum demands, that is, that the investor who places property in public use, as part of the railroad transportation system, while necessarily assuming the risk that in subnormal years he may not receive dividends, or even interest, and even under some circumstances not receive dividends during normal years, is entitled to protection against the confiscation and foreclosure for all time of his interest in property used and useful for the public on the basis of depression earnings.

When in 1939 the theory that the rights of investors in the railroads of the country should be cancelled and foreclosed for all time on the basis of past earnings was framed as an amendment of Section 77 in the so-called Wheeler Bill (S. 1869) and passed by the Senate, it was, after extended hearings before the Committee on the Judiciary of the House of Representatives, squarely rejected and the bill did not pass.

The Commission's Theory and Construction of Section 77

The Commission spells out its theory and construction of Section 77 in some detail in its reports in this proceeding. In its report of October 10, 1938, the Commission stated (R. 243):

> "It will be observed that **insofar as the capitalization of a reorganized company is concerned, section 77 contains no limitations other than that the fixed charges of the company shall be adequately covered by the probable earnings available therefor, and the plan as a whole shall be compatible with the public interest.** The public interest is not defined, but it would seem obvious that to be compatible with the public interest, the plan must provide a capital structure for the reorganized company which will give it a reasonable opportunity to function efficiently and continuously as a going concern. **This requires that the capitalization should not exceed a conservative appraisal of the assets to be taken over by the reorganized company,** and that proposed charges, whether fixed or contingent, be within its probable earning power."

The above statement is interesting in several respects. It gives frank recognition to the fact that the only express mandate of Congress as to capitalization is that fixed charges "shall be adequately covered by the probable earnings available therefor." It concedes that the Act does not further define, in express terms, its requirement that the plan as a whole "shall be compatible with the public interest." The Commission interprets the legislative requirement as to public interest to mean that a plan of reorganization must provide a capital structure for the reorganized company which will give it a reasonable opportunity to function efficiently as a going concern. From this the Commission spells out the two requirements that the capitalization shall not exceed a conservative appraisal of the assets to be taken over and that proposed charges,

whether fixed or contingent, be within its probable earning power. The Commission does not set forth the basis for its conclusion that contingent charges should be fully earned if the reorganized company is to function efficiently.

This statement by the Commission recognizes that a valuation of the property is essential. But in this case, the Commission made no revaluation; it proceeded to determine and limit the capitalization of the reorganized company without any reference to investment or to its Section 19a valuation of the property or any finding as to the earning power of the property.

After referring to the previous reorganization of the debtor, the Commission states (R. 244):

> "* * * If this reorganization is to be successful, the capital structure of the reorganized company must be realistically related to its actual earning power, and consideration given to the investment in its property only to the extent that such investment is justified by the probable earnings reasonably foreseeable for the future."

With the first part of this statement there would be little quarrel if the Commission were using "earning power" in the sense of the true legislative intent, as hereafter discussed in Point V of this brief. Unfortunately, the later part of this statement seems to indicate that the Commission means something far different from a willingness to consider investment where such investment is justified by earning power, in the sense of "capacity to earn." And throughout its reports the Commission discloses that it means something quite different in its use of "actual earning power" and "probable earnings reasonably foreseeable" from the meaning that may fairly be assigned to the phrase "earning power" as it appears in Section 77.

As will appear more fully from the pages which follow, the Commission completely abandoned the principles first

stated by it, that capitalization should be based upon a "conservative appraisal of the assets to be taken over by the reorganized company" and "related to its actual earning power," and proceeded to frame a plan of reorganization for the debtor on the revolutionary theory that the capital structure must be determined solely from a consideration of "probable earnings reasonably foreseeable for the future" and that total capitalization must be strictly limited in order to assure a material return upon the capital stock of the reorganized company from such probable earnings.

In its report of October 10, 1938, the Commission argues that the capitalization proposed by the parties is unsound, on the ground that the reorganized company could not earn enough to pay a dividend of five dollars annually upon its common stock (R. 256, 257; a dividend of three dollars annually is suggested at R. 269); and at a later point in its report the Commission states (R. 257):

> "* * * It is obvious, therefore, that based on the most optimistic estimate of earnings of record, the capitalization of the reorganized company must be maintained within strict limits if any material return on its capital stock is to be expected **and the shares of its stock are not to become mere tokens for stock market speculation.** It is true that considered alone, the data pertaining to the rate-making value of the debtor's property and its investment, would support capitalizations approximating those proposed in the three plans. We have hereinbefore stated, however, the reasons why, in our opinion, those factors can not be of controlling importance in a determination of the capital structure for the reorganized company. * * *"

The emphasized phrase "mere tokens for stock market speculation" which appears in the above statement of the Commission's position has an interesting history. It first emerged in the Wheeler-Lowenthal investigation of railroad holding companies. It later appeared in reports of the Interstate Commerce Committee of the Senate dealing

with the proposed amendment to Section 77 of the Bankruptcy Act which was passed by the Senate in 1939 and was rejected, after extended hearings, by the Committee on the Judiciary of the House. This proposed and rejected legislation, it should be noted, sought to amend Section 77 by substituting a determination of capital structure on the basis of earnings experience, for the valuation on the basis of "earning power" as it still appears in the Act. The phrase "mere tokens for stock market speculation" is a catch phrase, and, as used in the railroad holding company investigation reports, has some significance. The error here is that the Commission seized upon this catch phrase as an escape from the duties imposed upon it by a sound interpretation of Section 77 of the Bankruptcy Act. It has failed to regard the warning that this Court has given on several occasions in the past. In *Henneford* v. *Silas Mason Co.*, 300 U. S. 577, at page 586, this Court said:

> "* * * Catch words and labels * * * are subject to the dangers that lurk in metaphors and symbols and must be watched with circumspection lest they put us off our guard. * * *"

The Commission has never tried to explain further why its theory that a material return should be assured or expected on the capital stock of the reorganized company should, "in the public interest," take the place of "a conservative appraisal of the assets to be taken over by the reorganized company," to which the Commission refers in its report of October 10, 1938 (R. 243).

Any justification based on the argument that, if common stock of the reorganized company pays immediate dividends, it may prove a channel for future financing is completely negatived by the fact that the operation of the Commission theory at the present time is to foreclose the substantial rights of secured creditors, general creditors and stockholders in the property and, in effect, to confiscate

these rights on the basis of a mere theory of capitalization. No one thing could more clearly and certainly destroy common stock (or indeed, any railroad security) as a vehicle for future financing of railroad properties than this proposed action of the Commission.

At a hearing before the Special Subcommittee on Bankruptcy and Reorganization of the Committee on the Judiciary of the House of Representatives, on June 21, 1939, Chairman Eastman of the Interstate Commerce Commission stated (Report of Hearing, p. 553):

> "* * * To deprive thousands of investors who in the past have put their savings into railroad securities of all hope of recoupment is a very serious step, for if our capitalistic society is to succeed, it demands as scrupulously fair treatment of investors as of labor."

As a matter of fact, Congress in the enactment of Section 77 of the Bankruptcy Act was not dealing with problems relating to stock speculation. It was seeking to set up a legislative framework within which the existing investors in a railroad property, which had found itself unable to meet its fixed charges, could readjust its capital structure under supervision of the Commission and the courts. Congress, as will hereinafter be more fully stated, dealt with the public interest in relation to capitalization by expressly providing that the fixed charges under any plan of reorganization should be held within such limits that there would be adequate coverage for such fixed charges by the "*probable prospective earnings*" available for their payment. It did not charge the Commission with any mandate to so limit the capitalization proposed in the plan of reorganization that dividends on the stock of the reorganized company could be paid from probable earnings.

If Congress had remained silent as to the public interest in capitalization, the error of the Commission in its construction of the Act might seem to be a less clear

violation of the legislative mandate. But the mandate of Congress, that fixed charges only should be limited in the public interest by probable prospective earnings, appears clearly from the express language of the statute. Lured by a catch phrase, the Commission has sought to limit total capitalization arbitrarily and to deal with private interests in a confiscatory manner, and on a basis which finds no support in the language of Section 77 of the Bankruptcy Act.

In its supplemental report of June 21, 1939, in this proceeding the Commission expressly reaffirmed the position taken by it upon the question of capitalization in its prior report (R. 310):

> "In our prior report we stated that the entire capital structure of the reorganized company must be realistically related to its actual earning power, and in determining such capital structure consideration should be given to the investment in the property only to the extent that such investment is justified by the probable earnings reasonably foreseeable for the future if the reorganization was to be successful. With these considerations in mind, and for the reasons there set forth, and upon consideration of the investment of the debtor in its property, the probable rate-making value thereof, and its traffic and earnings, we conclude that we cannot approve the total capital structure under the Credit Corporation's proposed modification. * * *".

Thus, it appears that the Commission has abandoned completely the standard first stated above, that capitalization must be related to a "conservative appraisal of the assets to be taken over by the reorganized company," and has taken the position that the investment in the property is to be considered, in determining a proposed capital structure, only to the extent that it is "justified by the probable earnings reasonably foreseeable for the future." This is apparently intended as a reaffirmation of the Commission's basic theory, expressed in their October 10, 1938

report, that the capitalization must be kept within strict bounds in order to assure a material return upon the capital stock of the reorganized company.

In this connection, and especially as to the Commission's expressed desire to make "probable earnings reasonably foreseeable" the sole basis of the determination of a capital structure which will assure a material return on the stock, it is pertinent to quote further from the testimony of Mr. Eastman before the Committee on the Judiciary of the House on June 21, 1939, when he stated (Report of Hearing, p. 551):

> "Any estimate of the future earnings of a railroad can at best be no more than an 'educated guess,' but there has never been a time in the history of the country when it has been more difficult to make such a guess than now. Anything remotely approaching accuracy is impossible. * * *"

Basic objections to the substitution of capitalization theories for valuation under Section 77

At the outset the theory of the Commission that private property interests can be cancelled and foreclosed solely on the basis of an administrative finding of a desirable capital structure and without any finding or determination as to the value of the property interests or as to the value of the property of the debtor meets three obvious objections:

(1) The *du Bois* decision is against the Commission's theory:

This Court has unquestionably considered and rejected a contention that an approved capital structure may be substituted for findings or determinations of value in dealing with the rights of secured creditors. While *Consolidated Rock Products Co.* v. *du Bois*, 312 U. S. 510, arose

under Section 77B (now Chapter X of the Bankruptcy Act) and not under Section 77, it may fairly be urged as a square authority on the point here under consideration. In that case this Court had before it a plan of reorganization, which set up a definite capital structure, and which had been approved by the District Court as fair and equitable. This Court, after full consideration, clearly and definitely rejected the contention that an approved capitalization was an adequate substitute for findings as to the value of the property of the debtor when confiscatory treatment of private property interests was involved. It would be an anomalous situation if this Court should hold in this proceeding that the mere finding by the Commission that a certain capital structure was in the public interest justified the Commission in disregarding the clearly established value of the properties of the debtor, when the confiscatory treatment of a secured claim is at issue.

(2) Commission's theory conflicts with established principles of corporate law and accounting.

Any theory that the approval of a capital structure may be made a substitute for valuation of assets in dealing with private rights of security holders may also be said to fly in the face of the history and practice of corporate accounting. Surpluses and deficits are a commonplace of corporate accounting. Nowhere will one find a basis in established corporate and accounting practice for an assumption that capitalization may properly be taken as a measure of the value of the assets represented by the securities issued by a corporation. While the Circuit Court of Appeals for the Sixth Circuit has recently held in a case arising under Section 77 of the Bankruptcy Act (*Akron, Canton & Youngstown Ry. Co.* v. *Hagenbuch, et al.*, 128 F. (2d) 932, petition for certiorari filed August 31, 1942), that a finding by the Commission of capitalization may be accepted as the equivalent of a finding of value of

the debtor's properties, the opinion in the case does not attempt to support that conclusion by any reference to authority, logic or common sense.

This basis principle, that capitalization is a matter quite distinct from the value of the assets of a corporation, has been clearly recognized by this Court in other connections. In *Ray Consolidated Copper Company* v. *United States*, 268 U. S. 373, at page 377 this Court said:

> "The capital stock of a corporation, its net assets, and its shares of stock are entirely different things. Compare *Farrington* v. *Tennessee*, 95 U. S. 679, 686; *Tennessee* v. *Whitworth*, 117 U. S. 129, 136-137; *Wright* v. *Georgia R.R. & Banking Co.*, 216 U. S. 420, 425; *Des Moines National Bank* v. *Fairweather*, 263 U. S. 103, 111. The value of one bears no fixed or necessary relation to the value of the other. * * *"

(3) Commission's own plan of capitalization in this case negatives use of capitalization in lieu of valuation.

It is of considerable significance, and a basic objection to any use of capitalization as a substitute for valuation in dealing with private property rights in these proceedings, that the Commission has itself, apparently by deliberate intent, made it difficult or impossible to determine the dollars and cents limits of the capital structure for the debtor which it proposes in this proceeding. The Commission recommends that common stock without par value be used. The essence of stock without par value is that each share shall represent an aliquot interest in the assets of the debtor, subject to the claims of securities with priority. The Commission has, with apparent deliberation, refrained from putting upon this common stock without par value, any fixed value as of the time of issue. It has assigned a value of $57 a share to such stock in allocating shares to the First Mortgage bondholders and the Reconstruction Finance Corporation, one

of the secured creditors (R. 317). It has assigned a value of $62 a share to this stock in allocating shares to The Railroad Credit Corporation, also a secured creditor (R. 317). It has assigned no value to the common stock without par value which it has allocated to this respondent and the only guide as to the value of such stock is the express finding of the Commission that the stock so allocated is inadequate to satisfy in full the claim of this respondent (R. 269).

In addition, the Commission has at several points (R. 244, 245, 256, 259, 269, 321) in its somewhat discursive discussion in its reports of October 10, 1938 and June 21, 1939, referred to the common stock without par value as if it were to be assumed to have a value of $100 a share. Obviously, however, the Commission did not intend to have this regarded as an express finding of value for the common stock without par value. If it had made such a specific finding, then the aggregate value of the securities authorized would have exceeded by approximately $10,000,000 the total of the secured claims against the debtor (see tables on pp. 17 and 18). There could then have been no claim of justification for the failure of the Commission to refund the claim of this respondent in full.

The obvious difficulty in substituting a capital structure (including no par value stock) for a valuation in dealing with private rights is illustrated by the failure of the petitioners to agree on what the total capitalization does mean (Institutional Bondholders' brief, p. 55; Reconstruction Finance Corporation brief, p. 41).

There is no doubt that the Commission has interpreted Section 77 of the Bankruptcy Act as authorizing it to set up a scheme of capitalization solely with reference to "probable prospective earnings" and without any reference to a valuation of the property of the debtor on the basis of earning power, or to the investment in property dedicated to the public service, or to other relevant factors.

Reference to Powers of the Commission Under Section 20a of the Interstate Commerce Act Does Not Sustain Commission's Procedure

The petitioners have sought by an ingenious theory to justify and support the theory of the Commission that its determination fixing the total amount and character of the capitalization should take the place of findings of value for the properties of the debtor in dealing with private rights. By reference to the powers exercised by the Commission since 1920 under Section 20a of the Interstate Commerce Act, the petitioners contend that the Commission was vested with exclusive and plenary jurisdiction over the issues of securities of common carriers under Section 20a of the Interstate Commerce Act (49 U. S. C. A. § 20a) and that this jurisdiction has, by the provisions of Section 77 of the Bankruptcy Act, been extended so as to give the Commission exclusive and plenary jurisdiction to determine total capitalization and the classification thereof.

In substance, the contention of the petitioners is that the Commission is vested by Section 20a of the Interstate Commerce Act and Section 77 of the Bankruptcy Act with the same sort of exclusive jurisdiction to authorize security issues and determine total capitalization and classification thereof, and by inference, that its procedure here, under Section 77, is consistent with the long course of administrative procedure under Section 20a.

The contention of the petitioners amounts to a skillful translation of the power given to the Commission under Section 77, subsection (d) to approve a plan of reorganization which will, in its opinion, meet the express requirements of Section 77 (b) and (e) "and will be compatible with the public interest", into the assumed power to determine "total capitalization and the classification thereof" in the "public interest". In their contention they characterize the power of the Commission to regulate and con-

trol the issue of railroad securities as "exclusive and plenary"; and it was on this basis that the District Court in this proceeding refrained from any substantial exercise of its constitutional jurisdiction to protect private rights (Point VI below).

What are the facts as to the Commission's exercise of its powers over railroad securities and capitalization under Section 20a of the Interstate Commerce Act?

Section 20a (2) makes it unlawful for any railroad carrier subject to the jurisdiction of the Commission to issue securities or assume any obligation as lessor, guarantor, etc., unless the Commission authorizes such issue or assumption, and:

> "* * * The commission shall make such order only if it finds that such issue or assumption: (a) is for some lawful object within its corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the carrier of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purpose."

Subsection (7) of Section 20a provides:

> "(7) Jurisdiction of commission as exclusive and plenary. The jurisdiction conferred upon the commission by this section shall be exclusive and plenary, and a carrier may issue securities and assume obligations or liabilities in accordance with the provisions of this section without securing approval other than as specified herein."

Thus, by Section 20a(2) Congress granted to the Commission power to supervise and control the issue of securities by an interstate carrier, so that such issues would be for lawful objects which are within the corporate purposes of the carrier and "compatible with the public interest"; and by the terms of subsection (7) the jurisdic-

tion of the Commission is "exclusive and plenary" in so far as it comes in conflict with state regulations or legislation.

Three striking examples of the exercise by the Commission of the powers conferred by Section 20a appear upon the record in this proceeding:

(a) On November 20, 1930, upon application by The Western Pacific Railroad Company, the Commission granted to the Company authority to issue $5,000,000 of 5% Gold Debentures to be sold to the highest bidder at par, for the purpose of providing funds with which to complete construction of the Northern California Extension. The opinion of the Commission is set forth in the appendix in this brief at page xxvii. The Commission found (in the language of the statute):

> "We find that the proposed issue * * * (a) is for a lawful object within its [the Company's] corporate purposes, and compatible with the public interest, which is necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purpose."

At public sale, these debentures were sold to A. C. James Co. for cash at par and represent the original indebtedness upon which the secured claim of A. C. James Co. is based.

(b) On February 27, 1932, the Commission, again acting under the provisions of Section 20a, found that the value of the capital assets of The Western Pacific Railroad Company was $147,056,283, and that the excess of capital assets over liabilities was sufficient to justify, as compatible with the public interest, the proposed issue of $15,000,000 of General and Refunding Mortgage bonds and notes in the aggregate amount of $5,000,000 (R. 1060; appendix to brief, pp. xxxv-xxxvii).

(c) On December 9, 1932, the Commission granted authority to The Western Pacific Railroad Company to issue $4,000,000 additional General and Refunding Mortgage bonds, upon the basis of similar findings as to the capital assets of the company (R. 1060; appendix to brief, p. xlii).

These three examples of the Commission's exercise of its powers under Section 20a are typical of the Commission's action in exercising, or purporting to exercise, the powers granted to it under Section 20a of the Interstate Commerce Act.

Meaning of "compatible with the public interest" in Section 20a

The jurisdiction and powers of the Commission over security issues are clearly defined both in the reports of the Commission and in the decisions of the courts. The phrase "compatible with the public interest" acquired, long before the enactment of Section 77, a definite meaning.

This Court has held that this phrase, as used in Section 20a (2) of the Interstate Commerce Act, is related to the adequacy and quality of the public service, the economy and efficiency of the transportation service and facilities, and the protection of private property interests in relation to the issue of securities by public carriers.

In *New York Central Securities Co. v. United States*, 287 U. S. 12, the Court had before it an order of the Commission under Section 20a permitting the New York Central to assume obligations and liability in respect of the securities of certain leased companies. The opinion of the Court, by Mr. Chief Justice HUGHES, states that the term "public interest" used in Section 20a (2) (p. 25):

> "* * * is not a concept without ascertainable criteria, but has direct relation to adequacy of transportation service, to its essential conditions of econ-

omy and efficiency, and to appropriate provision and best use of transportation facilities, questions to which the Interstate Commerce Commission has constantly addressed itself in the exercise of the authority conferred. So far as constitutional delegation of authority is concerned, the question is not essentially different from that which is raised by provisions with respect to reasonableness of rates, to discrimination, and to the issue of certificates of public convenience and necessity. * * *"

The holding of this Court in the *New York Central Securities Co.* case, that the jurisdiction of the Commission was "exclusive and plenary," was made only in connection with a contention that the lease authorized by the Commission was beyond the corporate powers of the railroads under the laws of the state in which they were incorporated. The Court rejected this contention and held that the power delegated to the Commission by Congress excluded the exercise by the several states of control in this field of interstate commerce (287 U. S. at 27, 28).

There is no relation or connection between "compatible with the public interest" and "exclusive and plenary" other than the fact that the first phrase appears in subdivision (2) of Section 20a, and the latter, in subdivision (7). While Section 20a (7) excludes the exercise by the several states of control over security issues of interstate carriers, Section 77 does not exclude the exercise of their proper functions by state agencies (*Palmer* v. *Massachusetts*, 308 U. S. 79) and expressly preserves to the District Court its bankruptcy powers.

In *United States* v. *Lowden*, 308 U. S. 225, the Court again points out that the "public interest" in the consolidation or lease of carrier properties (under Section 5(4)(b) of the Interstate Commerce Act) "does not refer generally to matters of public concern apart from the public interest in the maintenance of an adequate rail transportation system" but is "to secure a more adequate and efficient transportation system."

And yet by some strained logic, the petitioners appear to find in the *New York Central Securities* case and in *United States* v. *Lowden, supra,* support for the contention that the well defined and well understood requirement of the "public interest" in the Interstate Commerce Act justified and supports their assumed standard of a capitalization in reorganization based in some undisclosed manner upon an unreported guess as to probable future earnings without basic findings of value, earning power, or other relevant facts, and without reference to the Court's constitutional power and duty to protect private rights.

There is no mystery as to the requirement of Section 77, subsection (d), that the Commission shall approve a plan which is "compatible with the public interest." This means that the plan as a whole must not be inconsistent with "the public interest in the maintenance of an adequate rail transportation system" (*New York Central Securities Co.* v. *United States*, 287 U. S. 12) or with "conditions of economy and efficiency" or with "appropriate provision and best use of transportation facilities" (*Texas* v. *United States*, 292 U. S. 522, 531; *United States* v. *Lowden*, 308 U. S. 225, 230).

It is obvious that the adequacy, efficiency or economy of a rail transportation system, or the best use of its facilities, will not be impaired by insistence upon determinations of earning power and value as a basis for the capital structure of a railroad in reorganization, or by giving full effect to the requirement of Section 77, that the District Court shall in passing upon the plan of reorganization exercise an informed, independent judgment.

The Commission's interpretation of its powers under Section 20a

In the practical interpretation of its powers under Section 20a the Commission has consistently adhered to the general standard stated in *New York Central Securities*

Co. v. *United States, supra.* In authorizing or withholding authorization for the issue of securities by railroad companies, the Commission has concerned itself primarily with preventing over-capitalization in relation to the actual investment in and value of the property of the carrier seeking authority to issue securities.

The basic principles under which the Commission, exercising its powers under Section 20a, has functioned in capitalization cases were announced in *Securities of Louisville & Nashville R. R.*, 76 I. C. C. 718 (1923). After stating that it would not permit full capitalization of all the assets of the carrier but would insist upon a reasonable cushion of uncapitalized assets, the Commission proceeded to indicate the assets which would be capitalized.

At page 720 it stated:

> "* * * We should authorize the capitalization of those assets of the carrier only which have been provided and which are intended for continuing productive use in the service of transportation. Such assets will be hereinafter referred to as 'capitalizable assets.'"

The Commission then discussed the capitalizable assets of the railroad, including working capital, materials and supplies, stocks of subsidiaries and other items and concluded (76 I. C. C. 726, 727):

> "The evidence establishes (1) that the applicant has a large uncapitalized surplus; (2) that its present capitalization is much less than its actual investment in property held for and used in the service of transportation, or any fair value of such property for rate-making purposes which we may hereafter fix under section 19a of the interstate commerce act; (3) that the increase in capitalization, which would result from the exercise of the authority to be granted herein, would still leave its capitalization below its actual investment in, and the probable fair value of, such property; (4) that its remaining uncapitalized surplus would be sufficient to serve the purposes for which a

surplus should be accumulated; and (5) that a larger stock base is necessary to enable it to issue sufficient bonds under its first and refunding mortgage to meet its future needs and at the same time comply with the requirements of the various State statutes referred to in our original report in this proceeding governing investments by savings banks and other investors."

Thus, it appears that the Commission squarely rests its determination of capitalizable assets, and the limitation on security issues in the public interest, on actual investment in property used in the public service and the fair value of such property as determined by the Commission's valuation proceedings under Section 19a of the Interstate Commere Act. The Commission requires, *first*, that the proposed issue of securities be adequately covered by the actual investment in the property of the carrier and, *secondly*, that it shall not be prejudicial to the adequacy, efficiency and general economy of the carrier's transportation services.

In subsequent cases the Commission has consistently adhered to this basis of capitalization and has permitted the issue of securities against the investment in carrier property, equipment, working capital, material and supplies, excepting certain types of assets which it has held not capitalizable.

Stock of Missouri-Illinois R. R., 131 I. C. C. 467 (1927);

Securities of Yankton, Norfolk & Southern R. Co., 154 I. C. C. 669 (1929);

Roscoe, Snyder & Pac. Ry. Co. Securities, 170 I. C. C. 403 (1931);

Missouri Pacific R. Co. Bonds, 180 I. C. C. 352 (1932);

Chicago, Milwaukee, St. P. & Pac. R. Co. Bonds, 193 I. C. C. 725 (1933);

Greyhound Corporation Issuance of Preference Stock, 1 M. C. C. 357 (1936);

Iowa Electric Light & Power Co. Securities, 247 I. C. C. 17 (1941);
Richmond, Fredericksburg & Potomac Dividend Obligations, 79 I. C. C. 465 (1923).

See also:

Delaware, L. & W. R. Co. Stock, 67 I. C. C. 426 (1921);
SHARFMAN, *The Interstate Commerce Commission*, III A, pages 506-514.

The meaning of "compatible with the public interest" as incorporated in Section 77, when enacted in 1933, must be construed to be the same as its meaning in 1932 when the *New York Central Securities* case was decided under Section 20a. There is clearly no language in Section 77 which would tend to expand the administrative construction given to the phrase under Section 20a in 1931 and 1932, when the issuance of securities to A. C. James Co. was approved by the Commission (p. 61, above).

This is not a case involving accounting entries where properties are actually purchased at a price

In cases where railroad properties have been actually purchased at a price, the Commission has limited the capitalization to the actual investment or price paid. It may be stated, therefore, that the authorized capitalization may not exceed either (a) the actual investment in the property, or (b) the value of the property as determined by an actual commercial transaction.

Atlanta, Birmingham & Coast R. Co. v. *United States*, 296 U. S. 33;
Securities of Louisiana Ry. & Nav. Co. of Texas, 99 I. C. C. 357 (1925).

These cases, and other similar cases cited by the petitioners, lend no support to the broad proposition that the

Commission's power over capitalization is "exclusive and plenary" in the "public interest".

In *Atlanta, Birmingham & Coast R. Co.* v. *United States, supra,* it appeared that the Atlantic Coast Line had acquired through a subsidiary (Atlanta, Birmingham & Coast Railroad) the assets of a small railroad in Georgia. The Atlantic Coast Line guaranteed the dividends on the preferred stock of the new company and agreed to pay approximately $4,248,000 in discharge of prior liens on the property, in consideration of the transfer to it of all the common stock. The Interstate Commerce Commission ruled that the common stock should be set up on the books of account of the new company at $4,248,000, which represented the "actual money cost" to the "accounting carrier". This ruling was pursuant to the accounting rules of the Commission. The railroad contended that it was entitled to use the 19a valuation by the Commission of the assets of the predecessor company in setting up such assets upon its books. The Commission then made an actual valuation of the properties and found the value equal to the par value of the preferred stock and $4,248,000 for the common stock, which in the aggregate was the "actual money cost", and required the new company to state its accounts accordingly.

This action was sustained by the Supreme Court, opinion by Mr. Justice Brandeis, on the grounds that (a) the accounting order was an administrative matter as to which the Court had no power to weigh the evidence; (b) that the report of the Commission showed ample evidence to support its valuation; and (c) that the actual money cost to the company provided an immediate and proper measure of value of the no par common stock.

It has been urged in this proceeding that the Supreme Court in that case upheld the Commission's rule that the value at which the property of the carrier should be entered on its books was the "market or fair cash value"

or the value for the purposes of sale and exchange. It is not stated by the petitioners that the properties of the carriers had been actually sold to the plaintiff on the dollars and cents basis required to be set up on its books of account, and that the Commission had actually found the value of the properties transferred to be equal to the par value of the preferred stock and the common stock authorized to be issued. In case of an actual sale as appeared in this case, it is not unreasonable that the property actually purchased should be capitalized at the purchase price, that securities should be issued only to the extent of the purchase price and that the property should be set up on the books of the purchasing company at the purchase price. This is the holding of the Court in the *Atlanta, Birmingham & Coast R. Co.* case.

The second point which the petitioners failed to state is that neither the determination of the Commission, nor the application of its accounting rules, nor the decision of the Court affected private rights or resulted in the destruction or confiscation of even one dollar of credit or claims or equity interest.

Summary

There would seem to be no escape from the conclusion that there has been a basic misconstruction of Section 77 by the Commission. It has sought to deal with private rights in a confiscatory manner, without reference to its prior determinations of the investment in the debtor's railroad system and its Section 19a valuation of such property, and without basing its decision on a proper exercise of its delegated function of redetermining the value of the debtor's properties on the basis of earning power and other relevant factors. It has been led astray from the clear path of sound statutory construction by a political catch phrase to the effect that stock, on which dividends cannot be paid, may become "mere tokens for

stock market speculation." On this basis it has sought to substitute a finding as to the amount and character of capitalization of the debtor for a finding as to the value of the properties of the debtor represented by that capitalization. On this basis the supporters of the Commission Plan have even urged that the Courts have no power to protect the property rights of this respondent and others, on the theory that the power of the Commission as to capitalization must be deemed to be "plenary and exclusive" and "in the public interest."

It may indeed be doubted that Congress itself could constitutionally enact a statute which purported to cut off a substantial part of the secured claim of this creditor by prescribing, in an alleged public interest, an amount and character of capitalization for the debtor.

The determination of the amount and character of capitalization has inescapable judicial aspects, affecting directly the property rights of this respondent with the result that the jurisdiction of the bankruptcy court cannot be completely ousted, either by the Congress itself or by any agency or authority of the legislature (*Ex parte Bakelite Corporation*, 279 U. S. 438; *In re N. Y., N. H. & H. R. Co.*, 16 F. Supp. 504; KATZ AND FRANKFURTER, *Federal Legislative Courts*, 43 Harvard Law Review 894).

One thing is clear, however: Congress did not give to the Commission a mandate under Section 77 to so proceed. Section 77 of the Bankruptcy Act was not enacted for the purposes of regulating security issues and insuring the payment of dividends on common stock, but for quite different purposes. It is the duty of the Commission to interpret and apply the statute according to the clearly disclosed legislative intent.

In its construction of Section 77 of the Bankruptcy Act it may fairly be said that the Commission has drifted away from the salutary principle set out by Judge Cooley in the third annual report of the Interstate Com-

merce Commission to Congress more than fifty years ago (p. 104):

> "* * * Undoubtedly the first duty of an administrative officer is to give effect to the law under which he acts. Much depends, however, on the manner in which this is done, and misdirected energy may render a law nugatory. * * *"

POINT III

The Commission's assumption of a legislative mandate under Section 77 authorizing it to convert valid debt into stock finds no support in the language of Section 77 and carries with it practical consequences seriously prejudicial to the credit of the debtor.

As is pointed out under Point II above, the Commission, in its report of October 10, 1938, in discussing the legislative mandate embodied in Section 77 of the Bankruptcy Act, clearly recognized that the only express provision as to capitalization was the clear-cut requirement of the Act that fixed charges should be limited so that they would be adequately covered by the "probable earnings available therefor." The Commission proceeded, however, to conclude, from the requirement that the plan as a whole must be compatible with the public interest, that this required "that proposed charges, whether fixed or contingent, be within its probable earning power."

It would seem obvious that the mere fact that Section 77 expressly provides, as a standard of public policy, that "fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads)" must be related to "probable prospective earnings" and adequately covered by the "probable earnings available for the payment thereof", shows beyond question that Congress did not intend that the same standard of public policy should be applied to contingent charges.

It would have been simple for the draftsmen to expand the phrase "fixed charges" to the phrase "fixed and contingent charges." The reason that Congress did not set up in Section 77 any such standard is obvious. The failure to earn fixed charges may lead to financial difficulties for a carrier and hence to a possible interruption of service to the public. A failure to earn contingent charges carries with it no such prejudice to the public.

In the Commission Plan, which is before the Court in this proceeding, the Commission, under the exercise of clear statutory power and authority, drastically limited fixed charges. It provided that the new company should issue no fixed interest obligations except a contemplated $10,000,000 of First Mortgage bonds to be issued to provide such new money as might be necessary in connection with the reorganization. No class of the existing secured creditors of the debtor, either First Mortgage bondholders or creditors holding obligations secured by General and Refunding Mortgage bonds, are to receive fixed interest obligations. It is interesting to note that no secured creditor in this proceeding has protested this drastic limitation upon the issue of fixed interest obligations. There was a clear public interest and a clear legislative mandate and it met with complete and unprotesting acceptance by all the parties to the proceeding.

The Commission, however, proceeding under its extension of the mandate of Section 77, to which reference is made above, drastically limited the issue of contingent or income bonds by the reorganized company. The existing First Mortgage bondholders, for instance, who now hold fixed interest obligations, are to receive under the Commission Plan only 40% of the face of their obligations in income bonds and the balance in preferred stock.

In a memorandum filed by this respondent with the Commission under date of January 11, 1937, it was pointed out to the Commission that its valuation of the physical

properties of the debtor's railroad system, made under Section 19a of the Interstate Commerce Act, with additions at cost to that time, amounted to approximately $145,000,000 and that the total funded debt of the debtor (exclusive of affiliated company open account advances and accrued interest) amounted to approximately $63,000,000, or less than 44% of the property valuation. It was urged upon the Commission that the relation of assets to total liabilities in the case of the debtor here concerned furnished no necessary basis for a change of any substantial part of the debt to equity. The memorandum referred to went on to state:

> "* * * Provided that the creditors are willing to surrender their demand for fixed interest on funded debt, as is essential in compliance with Subdivision (b)(4) of Section 77 of the Bankruptcy Law, there is no reason why their debt should not retain the character of debt upon the reorganization of the property.
>
> "The average investor who buys a bond wants to be a creditor and not the owner of an equity. Sometimes the preference is one of necessity because of the limitations of a trust instrument, or the limitations of law as to the character of the investments which certain institutions and individual fiduciaries may make. Sometimes it is mere personal preference. Whatever the basis, however, it seems clear that the investor should not be asked to change the character of his interest, unless the necessities of a sound financial reorganization make this essential.
>
> "It is respectfully submitted that there is nothing in the record here before the Commission which justifies the change in the character of the securities, held either by First Mortgage bondholders, or by secured creditors, from debt to equity."

The soundness of the contention in opposition to unnecessary changes of debt to equity, as urged upon the Commission, has been dramatically supported by recent developments in the field of taxation. The Commission, proceeding under an express desire to improve the credit of

a debtor railroad by a mandate that a secured creditor must accept for his interest bearing obligations, as here in the case of the First Mortgage bondholders, 40% of principal amount in debt and 60% in equity certificates, has created a situation where a large part of the money which the reorganized company will receive and which should be used in fairness and equity to pay interest on its obligations is siphoned off under the obligation of our Federal tax laws and becomes unavailable for the payment of interest justly owed.

Take the situation as to the debtor here. Neither in the calendar year 1940 nor in the calendar year 1941 did the debtor actually pay any Federal income taxes. Yet the brief for the Institutional Bondholders, at page viii of its appendix sets out a computation showing that, if in 1940 and 1941 the revised plan of capitalization proposed under the Commission Plan had been in effect, the debtor, on the same earnings basis, would have paid to the Federal Government taxes on a theoretical income after interest, exclusive of excess profits taxes, amounting to $1,248,641. This sum of almost a million and a quarter dollars should in fairness and equity be available to the debtor to discharge its obligations to its secured creditors for unpaid interest of prior years. But the Commission has said that sixty per cent of the debtor's bonds should be changed to stock "in the public interest", and this mere change in the form of security which they are to hold automatically prevents the debtor, to a substantial extent, from carrying out its obligation to pay its creditors interest lawfully payable.

If excess profits taxes are taken into account, the unjust effect of the Commission's theoretical extension of the public interest becomes more marked, and is a matter of general knowledge and concern among investors. Strangely enough, the petitioners purport to find in the increased taxes that would result from the Commission's capital

structure, to the injury of creditors, an argument in support of the Commission Plan.

There is probably no one influence which has been more potent in bringing railroad securities into general public disrepute and more effective in destroying the credit of railroads generally than the realization that the Commission is asserting a right under Section 77 of the Bankruptcy Act to prevent a debtor from having available the funds to pay the interest which it has contracted to pay to its security holders, by renaming a bond a stock in an alleged public interest.

POINT IV

Section 77 of the Bankruptcy Act does not delegate to the Commission authority to originate and impose upon the parties a plan of reorganization and to nullify completely the rights of the parties to propose and negotiate a fair and equitable plan.

When an administrative agency, with the accumulated prestige possessed by the Commission, writes an unsupported gloss upon a statute, its construction receives a surprising amount of non-critical acceptance. The briefs of the petitioners furnish examples of this.

At page 27 of the Reconstruction Finance Corporation brief the following statement occurs:

> "Under Section 77 Congress has delegated the primary responsibility for the development of the reorganization plan to the Commission, * * *."

Needless to say, the brief does not attempt to refer to what language in Section 77 supports this bald statement.

On page 48 of the brief for the Institutional Bondholders the following statement appears:

> "Section 77, as administered by the Commission, has substituted the Commission as the 'reorganizer' and its expert judgment for the old 'bargaining' among the securityholders. * * *"

The phrasing of this statement is illuminating. It does not assert that the language of Section 77 makes the Commission a "reorganizer". It does say that under Section 77, **"as administered by the Commission"**, the Commission has been substituted as "reorganizer". Surely, one may fairly ask, in view of the drastic change in reorganization procedure involved, and the tremendous burdens thus imposed on the Commission, that there be pointed out express language in Section 77 which makes the Commission a "reorganizer" and substitutes its fiat for any renegotiation of contractual relationships between the groups of security holders.

Again, at pages 118-119 of the Institutional Bondholders' brief, this expansive statement appears:

> "Indeed the new legislation, as has already been stated, created a procedure under which the Commission has **in effect** become substituted for the securityholders as the 'reorganizer' and its expert judgments substituted for the 'bargaining process' among securityholders for the determination in the first instance, not only of the over-all questions of public interest, such as the total amount and character of capitalization to be issued in the reorganization, but also of the financial and other factual problems affecting the distribution of that capitalization in accordance with the legal rights of the old securityholders."

The brief does not attempt to support this statement by reference to the language of the statute, but refers only to the former statement in the brief itself.

Developing the thesis that the Commission is required to "formulate" a plan of reorganization, the Institutional Bondholders' brief states, at page 124:

"The essential jurisdiction of the Commission under Section 20a is carried into Section 77 not only by the requirement that the Commission shall **formulate** a plan 'compatible with the public interest.' * * *"

And at page 131:

"By subsection (d) the Commission is vested with jurisdiction to *determine* a plan that will be compatible with the public interest. * * *" (Italics in the brief.)

Neither of these statements is supported by any reference to the language of Section 77 which would authorize the Commission to "formulate" a plan. Actually subsection (d) of Section 77 does not at all authorize the Commission to "determine" a plan; on the contrary the language is that the Commission shall *approve* or *disapprove* a plan.

Any construction of Section 77 which takes from the creditors and the equity owners the right to initiate by agreement among themselves a plan of reorganization, provided that such plan does not disregard the priorities of secured creditors and does not conflict with basic and well defined considerations of public interest, cannot be sustained under the language or demonstrable intent of Section 77.

The relations between various classes of security holders in a railroad property are contractual relationships. When uncontemplated factors (such as the impact of the 1929 depression) render it impossible that these contracts be performed according to their terms, the parties have an inherent right to renegotiate their contractual relationships.

There is no language in Section 77 which purports to take away from the parties this right of renegotiation. Even more clearly, there is no language in Section 77, which, on its face, gives to the Commission the power and the responsibility of framing plans of reorganization for railroads; and yet this is the practical effect of the construc-

tion of Section 77 of the Bankruptcy Act adopted by the Commission and applied in this proceeding.

A reading of Section 77 of the Bankruptcy Act as a whole indicates, of course, that it was the intention of Congress to extend the function of the Commission as to railroad reorganizations. The Commission itself had from time to time pointed out the difficulties which arose under the previously existing practice in equity reorganizations. It was said that plans of reorganization came before the Commission only after they were formulated and agreed upon by the parties and solely, under Section 20a of the Interstate Commerce Act, for action upon the authorization of the issue of new securities. Section 77 clearly accomplishes a contemporaneous supervision by the Commission and by the Court of the steps in reorganization with a view primarily to accelerating the reorganization of railroads as against the alleged delays of the old equity practice.

It is also clear that it was the Congressional intent in enacting Section 77 to limit, so far as it legally might, the opportunity of minorities to frustrate the formulation and putting into effect of a plan of reorganization.

The entire plan and scheme of Section 77, however, clearly indicates that the parties should propose a plan of reorganization and by negotiation and adjustment agree upon its essential features, within the framework of Section 77. Under the terms of Section 77, the debtor is made the moving party in submitting a fair and equitable plan to the court and to the Commission, but any creditor is entitled to submit a plan and there is express and detailed provision in the Act for agreement among the various parties in interest by formal vote.

Nowhere in the Act is there imposed upon the Commission an express power and duty to formulate a plan of reorganization. The Commission, however, has seized upon an almost parenthetical phrase, hereinafter quoted,

which appears in the first paragraph of subsection (d) of Section 77 of the Bankruptcy Act, as justifying an expansion of its powers. This phrase states merely that the plan approved by the Commission "may be different from any which has been proposed." The phrase in question actually appeared in parentheses in the original act, prior to the 1935 amendment. On the basis of this phrase, which should reasonably be interpreted to give a far narrower scope of authority to the Commission, the Commission has asserted a right in this proceeding to originate and impose upon the parties its own plan of reorganization.

When the Bureau of Finance of the Commission first formulated and released its proposed plan of reorganization, which rejected and disregarded all plans filed by the parties, every party to the proceeding filed objections to the proposed plan. When the Commission on October 10, 1938, issued this Bureau of Finance plan, with some modifications, as its plan of reorganization, every party to the proceeding filed objections and petitions for rehearing (R. 675 to 818).

The only parties in interest who are supporting this plan in this Court are First Mortgage bondholder interests (and as to the First Mortgage bonds, only those held by institutions whose interests may well be different in some respects from the interests of the average First Mortgage bondholder) and the Reconstruction Finance Corporation. The reason for such support is obvious. The Institutional Bondholders may well feel that they benefit, because of the complete priority granted to them by the Commission, from the cancellation or foreclosure of the interests of secured creditors, general creditors and equity owners.

The Reconstruction Finance Corporation is, under the Commission Plan, granted clearly preferential treatment in relation to other secured creditors and treated on a

parity with the First Mortgage bondholders. The fact that the Commission Plan has been supported in the courts by these two favored interests does not negative the fact that the plan here before the Court is a Commission Plan originated and promulgated by the Commission and resting not at all upon any proposal or agreement of the parties to the proceeding.

The language upon which the Commission bases its right to initiate and promulgate a plan is the clause which is emphasized in the following sentence taken from subsection (d) of Section 77 of the Bankruptcy Act:

> "* * * After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, *which may be different from any which has been proposed,* that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. * * *"

It is far more reasonable to assume that Congress intended by the language from subsection (d) of Section 77, italicized above, to make possible minor changes in the plan, consistent with the general intent and agreement of the parties, in order that reorganization might be expedited, rather than a broad grant of power to the Commission to originate and promulgate plans of reorganization. The language is reasonably calculated to meet any argument that the Commission must approve or disapprove a plan precisely as submitted to it and cannot condition its approval upon the making of definite modifications, which the Commission may find to be in the public interest and required by the express limitations set out in

Section 77. This is a far different thing from a broad grant to originate plans by administrative fiat.

If Congress had meant to give the Commission broad power to formulate plans of reorganization, it could (subject to obvious doubts as to whether such a delegation of right to interfere with the contractual freedom of the parties would be constitutional) have said so in clear and express language. Certainly it might well have omitted from the provisions of Section 77 the express and time-consuming provisions for the filing of plans with the Commission.

We shall have occasion in Point V, which follows, to indicate what seems to us to be the reasonable interpretation of Section 77 as to the relative functions of the security holders and the Commission in the formulation of a plan of reorganization.

POINT V

The groups of security holders represented in this proceeding should be permitted, under supervision by the Commission and the courts as contemplated by Section 77, to renegotiate their contractual relationships, and formulate and agree upon a plan of reorganization, which would (a) observe the rule of priorities of the *Boyd* and *du Bois* cases, (b) provide for fixed charges only to the extent that they shall be adequately covered by "probable earnings", and (c) provide for a total capitalization within the limit established by the value of the property of the debtor used in the public service, after due consideration of its earning power.

We have pointed out in Points II, III and IV, above, that the theory and construction of Section 77 by the Commission is not supported by the language of the statute, nor within the intent of Congress, and that it produced an

unfair and inequitable result when applied to the facts before it in this proceeding. We believe, and think it proper to so state at this point, that many of the difficulties and delays which have occurred generally in the attempt to reorganize railroads under Section 77, are to be attributed to the Commission's erroneous and impracticable construction of its functions and duties under Section 77.

Section 77 of the Bankruptcy Act was enacted in 1933 and substantially amended in 1935. It has not accomplished the purposes which prompted its enactment; that is, the improvement of the reorganization procedure as against the old equity practice. Since the enactment of the Act, three major railroad reorganizations have been effectuated under the procedure provided by Section 77. The three properties are:

The Erie Railroad System, 2,392 miles operated (see 239 I. C. C. 653 (1940), 240 I. C. C. 469 (1940), *In re Erie R. Co.*, 37 F. Supp. 237 (N. Dist. Ohio 1940));

Chicago & Eastern Illinois Railway, 925 miles operated (see 230 I. C. C. 199 (1938), *ibid* 571 (1939), opinion and order N. Dist. Ill. 1940, unreported);

Chicago Great Western Railroad, 1,502 miles operated (see 228 I. C. C. 585 (1938), 233 I. C. C. 63 (1939), 29 F. Supp. 149 (N. Dist. Ill. 1940)).

It is interesting to note that in the case of the three properties so reorganized, the Commission did not seek to foreclose or cancel the interests of creditors, secured or unsecured, and instead gave substantial recognition to the equity.

A number of small railroad properties have been reorganized under the Commission's interpretation of Section 77. Their aggregate mileage is relatively unimportant. These include such properties as:

Chicago, South Shore and South Bend Railroad, 90 miles operated (see 212 I. C. C. 547 (1936), 217 I. C. C. 423 (1936) opinion and orders, N. Dist. Ind. 1936, 1937, unreported);

Copper Range Railroad, 107 miles operated (see 212 I. C. C. 479 (1936) opinion and orders W. Dist. Mich. 1936, 1937, unreported);

Louisiana & North West Railroad, 99 miles operated (see 224 I. C. C. 58 (1937), 36 F. Supp. 636 (S. Dist. N. Y. 1938), *ibid* 639;

Reader Railroad, 22 miles operated (see 221 I. C. C. 190 (1937) opinion and order, W. Dist. Ark. 1937, unreported);

Savannah & Atlanta Railway, 147 miles operated (see 224 I. C. C. 197 (1937) opinion and order, S. Dist. Ga. 1938, C. C. H. Bankr. par. 51,448);

Spokane International Railway, 152 miles operated (see 228 I. C. C. 387 (1938), 233 I. C. C. 157 (1939), opinion and order, E. Dist. Wash. 1940, C. C. H. Bankr., par. 52,567).

It is a fair statement, however, that the major railroad properties, except the three mentioned above, which came into financial difficulties as a result of the impact of the 1929 depression, and as to which the reorganization procedure was invoked, are still dragging a laborious course through the Commission and the courts, mainly because of the Commission's unsound and unsupported interpretation of Section 77. These major properties, still in process of reorganization, include:

Chicago & North Western Railway, 8,319 miles operated (236 I. C. C. 575 (1939), 239 I. C. C. 613 (1940), 35 F. Supp. 230 (N. Dist. Ill. 1940), 126 F. (2d) 351 (C. C. A. 7th, 1942));

Chicago, Milwaukee, St. Paul & Pacific Railroad, 10,854 miles operated (239 I. C. C. 485 (1940), 240 I. C. C. 257 (1940), 36 F. Supp. 193 (N. Dist. Ill. 1940), 124 F. (2d) 754 (C. C. A. 7th, 1941));

Chicago, Rock Island & Pacific Railway System, 7,900 miles operated (242 I. C. C. 298 (1940), 247 I. C. C. 533 (1941));

Denver & Rio Grande Western Railroad System, 2,566 miles operated (233 I. C. C. 515 (1939), 239 I. C. C. 583 (1940), Finance Docket No. 11002, July 13, 1942, unreported, 38 F. Supp. 106 (Dist. Colo. 1940));

Florida East Coast Railway, 685 miles operated (Finance Docket No. 13170, April 6 and Aug. 10, 1940, unreported);

Minneapolis, St. Paul & Sault Ste. Marie Railway, 4,269 miles operated (Finance Docket No. 11897, March 17 and June 17, 1942, unreported);

Missouri Pacific Railroad System, 10,254 miles operated (239 I. C. C. 7 (1940), 240 I. C. C. 15 (1940), 39 F. Supp. 436 (E. Dist. Mo. 1940));

New York, New Haven & Hartford Railroad, 1,853 miles operated (239 I. C. C. 337 (1940), 244 I. C. C. 239 (1941), 16 F. Supp. 504, opinion and order Dist. Conn. 1941, unreported));

St. Louis-San Francisco Railway, 4,769 miles operated (240 I. C. C. 383 (1940), 242 I. C. C. 523 (1940));

St. Louis Southwestern Railway System, 1,650 miles operated (249 I. C. C. 5 (1941), 252 I. C. C. 325 (1942));

Central of Georgia Railway, 1,864 miles operated (Fifty-fourth Annual Report of the I. C. C., p. 58).

This respondent contends that while Section 77 of the Bankruptcy Act, as erroneously construed and applied by the Commission, has not worked well, the statute itself is wisely conceived and statesmanlike legislation. If given a reasonable interpretation, according to the true legislative intent, it would function fairly and efficiently and with much greater expedition than the old equity practice.

Only because of the unsound and unsupported construction which has been given the Section by the Commission, have defects arisen in its administration.

At the outset it should be noted that Congress itself has expressed clearly and without ambiguity in subsection (b) of Section 77 what it deems to be the basic public interest in capitalization. It has expressly provided that a plan of reorganization

> "* * * shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; * * *"

Congress meant just what it said in that provision; that it was the duty of the Commission and of the Court not to approve a plan unless its probable prospective earnings would clearly cover its fixed charges. It is the failure to earn fixed charges which carries with it the objectionable sequence of default on fixed interest payments and possible foreclosure of liens, with the resultant disastrous effect on credit and continuity of management. A failure to earn contingent interest, or dividends, creates no similar situation affecting vitally the public interest.

As to the elements of capitalization, other than those involving fixed charges, there is no evidence of any intent or purpose on the part of Congress to limit or restrain by the language of Section 77 of the Bankruptcy Act the freedom of negotiation and adjustment traditionally possessed by parties who have existing contractual relations and are called upon by economic circumstances to modify such contractual arrangements. On the contrary, there is every indication in Section 77 that Congress contemplated that

fair and equitable plans of reorganization would emerge mainly from agreement of the parties.

There is, of course, a necessary restriction inherent in Section 20a of the Interstate Commerce Act and expressly confirmed by Section 77 of the Bankruptcy Act, that the capital structure upon which the parties may agree shall be fully warranted by the capitalizable assets of the debtor and so entitled to approval of the Commission under its consistent and well established administrative practice under Section 20a of the Interstate Commerce Act. Subsection (f) of Section 77 contains an express provision to that end as follows:

> "* * * Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan and not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended. * * *"

Congress must be deemed in the enactment of the above quoted provision to have had in contemplation the established administrative practice of the Commission under Section 20a of the Interstate Commerce Act to which reference is made above in this brief at pages 59 to 69. That established administrative practice of the Commission was clearly that no securities should be issued which were not soundly based upon adequate capitalizable assets "intended for continuing productive use"[1] in the service of the public. It did not involve or contemplate any attempt to restrict the issue of equity securities in order that a material return might be expected upon such stock. (See quotation from Commission's report of October 10, 1938, appearing at page 51, above.)

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[1] *Securities of Louisville & Nashville R. R.*, 76 I. C. C. 718, 720 (1923).

It is obvious that the interpretation and application which the Commission has given to Section 77 in this proceeding has rendered completely nugatory the provision in Section 77 for the valuation of the property of the debtor. That provision occurs as the last paragraph in subsection (e) of Section 77 and reads as follows:

> "If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

A revaluation of the debtor's property by the Commission may not be necessary where the parties can arrive at a plan of reorganization which gives due recognition to the rights of each class of creditors and stockholders, and otherwise complies with the limitations of Section 77, but it needs no extended argument to point out that a valuation of the property of the debtor is essential before the property rights of a secured creditor can be foreclosed and this is what is attempted in the plan here before this Court. It is also obvious that the rights of general creditors and of equity owners can be held to be without value only on the basis of a valuation of the assets of the debtor in which such general creditors and equity owners have an interest.

The very language used in the quoted paragraph from subsection (e) of Section 77 of the Bankruptcy Act negatives the validity of the interpretation which the Commission has sought to give to the Section. The Commission has

tried to foreclose the interests of secured creditors and unsecured creditors and the equity on the basis of a capitalization determined solely with reference to "probable earnings reasonably foreseeable for the future" (R. 244, 310). To be sure, the Commission does not squarely find in its reports in this proceeding what the probable prospective earnings of the debtor are. More important, however, is the fact that Congress has expressly provided that the value of the properties of the debtor, which value is necessarily reflected in the values to be assigned to its securities, must be based, not upon "probable earnings reasonably foreseeable", but upon quite a different thing: "earning power".

"Power" is generally and properly defined as "capacity to produce an effect". "Earning power", as used by Congress, necessarily means "capacity to produce earnings". That is quite a different thing from "probable prospective earnings", which is interpreted by the Commission to mean earnings that are reasonably foreseeable for the immediate or near future.

Respondent earnestly contends that the above quoted language from subsection (e) of Section 77 of the Bankruptcy Act must be construed in the light of the knowledge by Congress that the Commission had, at great expense to the public and to the carriers, prepared and promulgated valuations of the properties of the carriers under Section 19a of the Interstate Commerce Act which valuations accurately disclosed the true investment of the carriers in their properties, and readjusted such valuations to exclude unwarranted capital expenditures and abandoned properties, and kept these valuations up to date by the record of additions and betterments made under Commission supervision.

The emphasis in the quoted language on earning power, construed as capacity to earn, clearly authorized and directed the Commission to make such modifications in its

valuations made under Section 19a of the Interstate Commerce Act as would take into account those situations where an actual investment in railroad property did not properly reflect a capacity to earn under present conditions, or for the future, either because of permanent changes in traffic conditions or because the industrial decline of areas served had diminished the economic usefulness of the properties, or where the original investment had been ill-conceived and did not represent such potential service to the public as would give the property a capacity to earn commensurate with the investment.

The legislative history of the enactment of the 1935 amendment to Section 77 of the Bankruptcy Act supports the view that Congress meant no more by the language it uses as to the basis of valuation in subsection (e) of Section 77 than such express extension of power to the Commission, where necessary, to revise and modify, for reorganization purposes, its prior valuations of the railroads, with full consideration of "earning power", in the sense of "capacity to earn" based on the usefulness to the public of such property. From this point of view, the concept carried into Section 77 is closely akin to the much discussed doctrine of "prudent investment", enunciated by Mr. Justice Brandeis when a member of this Court (*Southwestern Bell Telephone Co.* v. *Public Service Comm.*, 262 U. S. 276, 289).

The 1935 amendment to Section 77 of the Bankruptcy Act was separately introduced in the House of Representatives and in the Senate. Neither in the House nor in the Senate was there discussion on the floor as to the significance of the phrase "earning power" as it appears in the valuation provisions of subsection (e) of Section 77. When the House bill was before the Committee on the Judiciary of the House of Representatives, Mr. Leslie Craven, counsel for the Federal Coordinator of Transportation and accredited draftsman of the proposed legislation, appeared

on April 15 and April 16, 1935, before the Committee to outline the intent and purpose of the proposed amendment to Section 77 of the Bankruptcy Act. Throughout his presentation to the Committee on the Judiciary there appear statements which are illuminating as to the true significance and intent of the phrase "earning power" as used in Section 77. The language quoted below is that of Mr. Leslie Craven, except where otherwise indicated in the case of members of the Committee on the Judiciary of the House of Representatives:

Page 28 report of hearing before the Committee on the Judiciary of the House of Representatives

"If you have built a Mayflower Hotel in Alexandria and it is not able to make operating expenses, what it cost does not have anything really to do with the case, because that is not even evidence of the probable value of that property.

• • • • • • • • • •

"If you will excuse me I think that this is sufficiently important to read:

'For the purposes of any determination in proceedings under this section to which the fair valuation of any property used in railroad operation—'

"That is important; this would not apply to land which was held for investment purposes. [Reading:]

'may be necessary, including, but not limited by, the solvency of the debtor, such valuation shall be determined on a basis which will give due consideration to the earning power of the property, present and prospective, and all other relevant facts.'

"That is the law as we understand it for the determination of the kind of value which is here in issue.

"Personally I think that prospective earnings are the things which are the most important and you will

observe that we are talking about 'earning power'. We are not proposing that we organize these railroads on the basis of present earnings. You could not do it. The roads now either in bankruptcy or equity proceedings are only earning one-seventh of their bond interest."

Page 31

"For that reason, to be quite frank with you about the matter, this rule is not an entirely satisfactory rule, because it is not precise. It is not as definite as you would like to have it, but we do not know any way to get a more definite rule.

"This is legally sound; that is, I mean that it puts emphasis, as it ought to, off of costs and on to earnings.

"Now, we have to leave that to the determination of the court and the Commission. We do not think that it is wise to try to straightjacket that thing, by telling them how they shall do it, and we do not believe, let me say, that under this rule this Interstate Commerce Commission is going to take that provision and use it in a senseless way, that is, in a way whereby they would, for example, reorganize these railroads on the basis of these obviously subnormal present earnings.

"In getting up a statute like this, you have to count on the intelligence of your administrative agency, and you cannot legislate intelligence into it.

"Now, what I have said has largely to do with provisions designed to enable the putting through of plans, when times are propitious, with fair treatment of equity interests and in a manner not to permit their obstruction for purposes of driving a better bargain."

Page 38

"There is not any question, I believe—at least serious question—that in the determination of value for reorganization purposes, the weight must be given to the actual economic value of the property. That

is its worth. And, as I illustrated yesterday, if you should unwisely do what thousands of people have done, invest large sums in boom times in such a thing as a Mayflower Hotel located over in Alexandria, it cannot be expected, in the very nature of things, that if that property becomes insolvent, or unable to meet its bills, when it is reorganized, it shall be again organized on the basis of the investment or the reproduction cost at present prices. That is an absurdity on the face of it."

Page 39

"Another point is this: We set up in the last provision of that paragraph a rule of evidence; evidence of these respective kinds of cost figures shall not be received unless it shall be first established that in the light of its earning capacity, which we regard as the true measure of value, and all the other relevant facts —we do not exclude anything; we let the court look at the whole proposition—such sums as are evidenced by such reproduction or original cost of, or actual investment in, the property could, at the time of the proceeding or within a reasonable period thereafter, be reasonably invested therein.

"In other words, you cannot bring in testimony and prove, over months of time, with all of the labor that is required to make such proof, these investment and reproduction cost figures, unless you first establish that the sum claimed in that way could be reasonably invested.

"'Reasonably invested' is merely another way of saying that you could get a return on it in a reasonably near future period. Our authority for that is the following case, and I submit it to you as a bit of sound reasoning. It is a decision of the circuit court of appeals in *United States* v. *Boston & New York Canal Co.* (271 Fed. 877, at 889), which was a condemnation case."

Pages 40 and 41

"The point there is this: That the value that was in issue before the Interstate Commerce Commission was a value for rate-making purposes and it was based

on cost figures; because when you come to make rates on the basis of value you cannot take earnings and capitalize them, because if you do you get into a vicious circle. Therefore a value for rate-making purposes such as was found by this Commission produces a sum which, with reference to its actual value, is often tremendously in excess, because it is primarily a cost figure.

"Their effort was to ascertain as well as they could by the use of reproduction-cost figures an approximation of what they thought was probably the proven investment."

Pages 42 and 43

"Take my hotel down there in Alexandria, my Mayflower Hotel. The reproduction cost of that property at 1928 prices ought not to be received in evidence unless somebody can show that under the reasonable and prospective earnings of that property a sensible man would make that investment. Now, we are not trying to be hard-boiled about this thing. This was not an effort to be harsh. This will be objected to, you will find, by the equity holder."

Page 43

"Now, this could be done: It would be perfectly constitutional. It would be a provision that a road would be regarded as insolvent, so that there would not be the necessity of submitting a plan to stockholders, in the event that the earnings available for the payment of dividends on that stock, for a period of, say 5 years had not been adequate to pay any dividends. Under the law, there is not the slightest doubt that the Congress—it has been decided in many cases—has latitude in the fixation of its definition of insolvency. That provision would be proper. Now, if there is anyone who thinks that this valuation provision is not what it ought to be, then the substitute for it is a provision of the kind which I have suggested, which would be very effective.

"Mr. Michener (a member of the Committee on the Judiciary). It would be very effective in wiping out all equities in any kind of business in the country.

If business has got to be measured by its earnings in the last 5 years—any business, I do not care what it is—it would be just about as unfair a thing as could be imagined or suggested.

"Mr. Craven. And that is why we did not adopt it. I think this is a fairer standard.

"Now, I will say this with reference to this valuation provision. I brought it up here for discussion because it is an essential and important part of this act. But I do not think that it will attain any such importance in an actual reorganization, as you might suppose, from the conversation that has been had here, because what will happen will be that they will come in with a plan, it will be considered as to whether it is reasonable, and the valuation determination will be apt to be a secondary thing, not a primary thing.

"I do not think the court ought to—if I were a judge I would not, and I am sure you would not—sit down and say in a coldblooded way, 'Well, now, gentlemen, we are going first to fix a valuation.' I would consider the plan first. That is what the courts are going to do."

It may be conceded that Mr. Craven has subsequently made many public statements about the meaning of the valuation clause in Section 77, which might be urged as inconsistent with the excerpts set out above. There is, for instance, his explanation of the clause, which somewhat surprisingly was quoted with approval by the District Court in its opinion approving the Commission's theory of capitalization and its resulting Plan, as follows (R. 1584):

"* * * the valuation provisions in the existing law were so drawn that whoever tried to upset the valuation of the Commission would not be able to do it. The language is left in generalities. * * *"

However, what Mr. Craven said subsequently is of little importance; what he said to the House Committee, in ex-

plaining the purpose of the provision in his capacity of accredited draftsman, and during the consideration of the 1935 amendment, is of considerable importance as bearing upon the legislative intent.

In the proceeding here under review, the Commission deliberately avoided making any findings as to the valuation of the property of the debtor other than its finding under Section 19a of the Interstate Commerce Act which it incorporated in its report of October 10, 1938 (R. 224). That valuation was, as indicated above (Point I), adequate to justify the recognition of the secured claim of this respondent in full, with ample margin over for the general creditors and the equity. The Commission did in its report use discursive language expressing a doubt as to whether the original line of railroad of the debtor, which is the nucleus of its present railroad system, represented initially a prudent investment on the part of the Denver and Rio Grande Railroad Company (R. 244), which fell into financial difficulties because of that investment. It is obvious, however, that the Commission could not have found on the record before it that the present railroad system of the debtor was not a property essential to the efficient functioning of our national transportation system.

In this connection and as bearing upon the economic justification for the debtor's railroad system, attention of the Court is called to the tabulation which appears in the record as Exhibit L, annexed to the stipulation filed by the parties in the District Court (R. 1267-8). This table is reprinted for the convenience of the Court at page LIV in the appendix to this brief.

This table shows that even during the depression years the traffic burden borne by the debtor's railroad system for the benefit of the public has steadily increased in an impressive manner in ratio to the increase of traffic on

other Class I carriers. While undoubtedly, the present high level of gross earnings may be attributed in part to war conditions, it is more largely attributable to the developments in the debtor's railroad system and connections with it, which are discussed above at pages 27 to 29 of this brief. The fact that the debtor's railroad system is carrying its share of the burden of war traffic merely helps to demonstrate that its properties represent an essential investment in the public interest. That it has a capacity to earn at least commensurate with its investment valuation as found by the Commission under Section 19a of the Interstate Commerce Act is clear beyond doubt.

If the Western Pacific Railroad System, as now constituted, did not exist, the public interest would make desirable its present construction if this were possible under existing conditions. There is no doubt that the earning power of the property today fully justifies the valuation on the investment basis found by the Commission in its 19a proceedings. The actual earnings of $4,548,138 available for interest during the calendar year 1941 and of $7,987,512 available for interest for the year from August 1, 1941 to July 31, 1942, as discussed above at pages 24 and 25 of this brief, are an adequate practical demonstration that the property has a capacity to earn commensurate with its Section 19a valuation as found by the Commission.

No reasonable ground can be found in the record before this Court to justify a refusal on the part of the Commission to allow the parties to the proceeding to agree upon a plan of capitalization acceptable to creditors and stockholders, providing the limits of such capitalization fall within the 19a valuation as found by the Commission, after application of full accrued depreciation on roadway and structures as well as on equipment.

The Commission's "realistic" construction of Section 77

The Commission in its reports leans heavily upon the word "realistic" to characterize its proposal to substitute in its Plan a limited capital structure for determinations of value and earning power. For example, in its report of October 10, 1938 (R. 244) the Commission says:

> "* * * If this reorganization is to be successful, the capital structure of the reorganized company must be *realistically* related to its actual earning power, and consideration given to the investment in its property only to the extent that such investment is justified by the probable earnings reasonably foreseeable for the future."

The Commission's basic assumption is that all the ills of the railroad industry can be cured and the credit of the railroads assured, by revising downward the capitalization of the railroads, on the basis of depression earnings, so as to foreclose the interests of investors, including secured creditors, to the end that dividends may be assured on the new common stock. To characterize any such theory as "realistic" involves a sad straining of the ordinary meaning of the word. A more doctrinaire approach to the problems of the railroad industry could hardly be conceived.

It amounts to saying that every investor in railroad property placed in the service of the public takes the risk, not merely of not receiving interest or dividends during depression periods, but also of having his entire investment cancelled and foreclosed for all time on the basis of such depression earnings or forecasts based upon such depression earnings. When an attempt was made to legislate this theory into Section 77, as an amendment in 1939 (see S. 1869 and Report of Hearings before the Special Subcommittee on Bankruptcy and Reorganization of the Committee on the Judiciary of the House), the

theory was properly rejected by the Committee on the Judiciary and the proposed amendment failed of enactment.

The sound construction of Section 77

A sounder and more realistic interpretation of Section 77, and one supported by the language of the statute, would be to hold that the legislation was intended to facilitate the reorganization of railroads in distress, under regulatory supervision of the Commission and the Courts, rather than to delegate to the Commission alone the power and the responsibility of formulating plans of reorganization under economic concepts which find little or no support in the language used by Congress.

We contend that Section 77 of the Bankruptcy Act clearly contemplates that the parties in interest, creditors and stockholders, should be given an opportunity to renegotiate and adjust their contractual relationships, which have been disturbed by the failure of the property to earn its fixed charges under depression conditions. This right to renegotiate is, admittedly, subject, under the language of Section 77 of the Bankruptcy Act, to certain definite limitations.

In the first place, the plan of reorganization submitted must be "fair and equitable"; this necessarily means, among other things, that under the rule of the *Boyd* case, as reenunciated by this Court in *Consolidated Rock Products Co.* v. *du Bois, supra,* the priority rights of secured creditors must not be impaired.

In the second place, the proposed plan of reorganization must not provide for fixed charges in excess of an amount which is fully covered by "probable prospective earnings." The Commission is expressly charged under the terms of Section 77 with regulatory authority to assure

that no plan be put into effect which violates this limitation. A reasonable corollary of this clearly expressed legislative intent (although not so clearly expressed in the language of the statute) is that income bonds provided for by a plan of reorganization should be long term, and not short term securities, so as to avoid imposing upon the property the equivalent of fixed charges and the possibility of default upon its obligations within any reasonable period in the future.

In the third place, the total capitalization contemplated by the plan of reorganization must be within the amount of capitalizable assets turned over to the new company. Section 77 of the Bankruptcy Act is quite clear in supporting the standard as to capitalization which has been applied by the Commission since 1920 in the authorization of the issue of securities under Section 20a of the Interstate Commerce Act. (See discussion as to Commission's established administrative practice at pp. 59 to 69, above.) All that the valuation provision appearing in subsection (e) of Section 77 of the Bankruptcy Act can reasonably be interpreted to mean is that the Commission is authorized to revise its 19a valuation (which is substantially on an investment basis) where basic changes in economic conditions or other circumstances have permanently reduced the earning power of the assets devoted to the public service.

Practical application of Section 77 to the situation presented in this proceeding

The parties to this proceeding did not agree upon a plan of reorganization, and unite in urging it upon the Commission. Three separate plans of reorganization, and a number of modified plans, were filed with the Commission by the parties to this proceeding. All three plans submitted by the parties contemplated the refunding in full of the secured claim of this respondent. All three of these plans were rejected by the Commission on the ground

that they contemplated capital structures which the Commission regarded as in excess of that capital structure which they deemed should be created "in the public interest."

This respondent submits that within the fair contemplation of the legislative intent of Section 77, in the light of the facts before the Court, the parties should be permitted to agree upon a fair and equitable plan of reorganization which would:

(a) fully preserve the rights of priority of all creditors;

(b) contemplate a capital structure clearly within the limitation of properly capitalizable assets as determined by the 19a valuation made by the Commission (which in view of the demonstrated earning power of the present property of the debtor should not be reduced on any theory of loss of economic usefulness for the service of the public);

(c) contemplate (as does the Commission Plan) the complete elimination of all fixed charges except to the limited extent that it may be necessary to issue obligations for new money;

(d) preserve original debt as debt, on a contingent or income basis so far as interest is concerned, and on a long maturity basis so that the ability of the enterprise to function continuously for the future shall be assured against any danger arising from possible default on either fixed interest obligations or near maturity of income obligations; and

(e) avoid any unnecessary confiscation of property rights of secured creditors (such as this respondent), general creditors or equity owners, represented by investment in property fully used and usable in the public interest.

If the parties to this proceeding are allowed to renegotiate and adjust their contractual relationships within the clearly expressed limitations imposed by Section 77 and are relieved from the unreasonable limitations of the unsound economic theories which the Commission has sought to impose upon Section 77 as a gloss, it is submitted that an agreed plan of reorganization can be worked out and made effective without loss of time. Only if the parties are free from the limitation upon total capitalization proposed by the Commission can a plan be framed which is truly "fair and equitable" within the express requirements of Section 77.

What is here proposed involves no long drawn out valuation proceeding before the Commission or in the courts. The Commission has, as disclosed in its reports in this proceeding, full data as to the investment of the debtor in its properties and as to the Commission's own valuation of the properties under Section 19a. This latter valuation excluded and disregarded a substantial part of the debtor's original investment as representing excessive construction costs (*Western Pacific Ry. Co.*, 29 I. C. C. Val. Rep. 239, I. C. C. Exhibit 104, R. 2498, unprinted record). This valuation data has been kept currently up to date by the Commission through its exercise of its regulatory powers as to the debtor's additions and betterments and its accounting. There is obviously no need in this proceeding that the Commission should substantially readjust downward, for the purpose of determining the total allowable capitalization, its prior valuations of the properties of the debtor, by giving further consideration to "earning power" as authorized by subsection (e) of Section 77. The present actual earnings of the debtor's properties are a complete and irrefutable demonstration that those properties have a "capacity to earn" fully commensurate with the Commission's prior Section 19a valuation.

POINT VI

The District Court in this case failed to exercise an informed and independent judgment in approving the Commission Plan.

The Circuit Court of Appeals for the Ninth Circuit in its opinion has pointed out (R. 2672-4) that the District Court in passing upon the Commission Plan misconstrued and improperly limited its judicial functions under Section 77 of the Bankruptcy Act. Because of the District Court's misconception of its functions no adequate review of the Commission's determinations was possible, and judicial questions affecting private rights have not been decided.

The theory of the District Court

The opinion of the District Judge discloses the premises upon which he relied in dismissing all objections and approving the plan of reorganization of the debtor which was formulated and certified by the Commission. The opinion states (R. 1596):

> "• • • The determination of the amount and character of the capitalization (a legislative function affecting the public interest) is exclusively within the province of the Commission. The only qualification, if any, is that the court shall independently determine whether, in the exercise of its jurisdiction, the Commission has acted fairly, within the bounds of the Constitution, and not arbitrarily. The determination of the questions relating to the distribution of the new securities, including legal priorities and allocations, involves private rights and is a judicial function, within the province of the court. • • •"

The District Court does not tell us by what authority this division of issues is made—"amount and character of capitalization" to the Commission, "distribution of new

securities" to the Court. The phrases themselves do not appear in Section 77, 77B or in Chapter X of the Bankruptcy Act. Subsection (e) of Section 77 expressly directs the Court to approve the plan only if satisfied that it meets the requirements of the statute, and is fair and equitable, non-discriminatory and in conformity with law.

Even as to the issue of the "distribution of the new securities," as to which the District Court accepted a judicial responsibility, the opinion of the District Court shows complete surrender to "the experience, ability and specialized knowledge" of the Commission (R. 1588), and a complete acceptance of its preliminary determination of questions relating to the distribution of the new securities (R. 1597), which was of "inestimable value to the court" and with which the Judge was "wholly in accord". Hence, "further discussion would be superfluous. Every question presented by the objections was considered and passed upon by the Commission as shown by its original and supplemental reports" (R. 1597).

Thus, it appears that, as to questions of capitalization, the District Court refused to pass judgment. As to questions of distribution, the stated acceptance of judicial responsibility was not accompanied, so far as can be spelled out from the opinion of the District Court, by more than a merely superficial review of the Commission's prior determinations.

This judicial renunciation should be compared with the standard indicated by the words of Mr. Justice Douglas in *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, 115 (under 77B), where this Court rejected the contention that the approval of a plan of reorganization by the great majority of security holders relieved the reorganization court of the duty to make an independent determination as to the fairness and equity of the proposed plan. The Court said:

"* * * The contrary conclusion in such cases would make the judicial determination on the issue of fairness a mere formality and would effectively destroy the function and the duty imposed by the Congress on the district courts under § 77B. That function and duty are no less here than they are in equity receivership reorganizations, where this Court said, 'Every important determination by the court in receivership proceedings calls for an informed, independent judgment.' *National Surety Co.* v. *Coriell*, 289 U. S. 426, 436."

This principle was reaffirmed in *Consolidated Rock Products Co.* v. *du Bois*, 312 U. S. 510, at page 520.

Under these decisions and the doctrine of the *Boyd* case, questions of the amount, character and distribution of new securities must be scrutinized by the District Court, notwithstanding the prior approval of the overwhelming majority of the security holders. Can the duty of the Court be less where the determination of capital structure and the distribution ordered by the Commission, without the consent of security holders, cuts off property rights of secured creditors?

Public interest and private rights are intertwined in a reorganization proceeding. The District Judge in this proceeding, by arbitrarily excluding the most important issue from his consideration, has denied a proper judicial hearing on the plan of reorganization. This abdication of judicial power and refusal to perform the Court's duty is justified neither by logic nor by authority nor by the provisions of Section 77.

In any consideration of any plan of reorganization the question of amount and character of new capitalization is a question to be determined. It is involved in an equity receivership, in a reorganization under Section 77B or Chapter X and in a reorganization under Section 77. In any reorganization this determination affects private rights as well as the public interest. Section 77 does not withdraw the consideration of this issue from the District Court.

A Reorganization Proceeding under Section 77 is a Judicial Proceeding in Bankruptcy.

Section 77 of the Bankruptcy Act is a law on the subject of bankruptcies, enacted by Congress under its power to legislate upon that subject.

Continental Illinois National Bank & Trust Co. v. *Chicago, Rock Island & Pac. Ry. Co.*, 294 U. S. 648;
Palmer v. *Massachusetts*, 308 U. S. 79.

In *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pac. Ry. Co., supra*, the Supreme Court held that Section 77 conferred upon the bankruptcy court jurisdiction to enjoin creditors, who held notes of the debtor railway secured by its bonds and the bonds of its subsidiaries, from selling the collateral under the power of sale in the notes, and that this grant of power was a constitutional exercise of the bankruptcy power. This decision involved the Section as enacted in 1933, prior to the 1935 amendments which added the valuation provision and made numerous other changes.

The companion Section (Section 77B, now Chapter X of the Bankruptcy Act), has also been held valid as an exercise of the bankruptcy power.

Kuehner v. *Irving Trust Co.*, 299 U. S. 445;
Campbell v. *Alleghany Corporation*, 75 F. (2d) 947; certiorari denied, 296 U. S. 581.

An order confirming a plan of reorganization under Section 77B is an order in a "proceeding in bankruptcy" (*Meyer* v. *Kenmore Hotel Co.*, 297 U. S. 160).

A reorganization proceeding under Section 77 must be initiated by a petition filed with the District Court and approved by the judge. Thereupon, by the express

provisions of subsection (a), the Court is vested with "exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose."

Subject only to express provisions of the statute, the powers and duties of the court in a reorganization proceeding under Section 77 are the same as the powers and duties of the bankruptcy court in an ordinary bankruptcy proceeding. It is so provided in subsection (l) of Section 77:

> "In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

Section 77 Does Not Curtail the Judicial Powers of the Bankruptcy Court.

The statute does not attempt to subject the District Court to the power and control of the Commission, or to make the Court a reviewing body or to confer upon the Commission the judicial powers of a bankruptcy court (*In re New York, N. H. & H. R. Co.*, 16 F. Supp. 504).

Under the statute only the judge may dismiss the proceedings upon the filing of the original petition, after approval of a plan by the Commission, or after certification of a plan by the Commission. While no plan shall be approved or confirmed by the Court unless it has first been approved by the Commission, the order of the Commission approving a plan is merely a jurisdictional prerequisite and is of

no force and effect unless and until the plan has received the independent approval of the Court after a judicial hearing upon the objections and claims of the parties (*In re New York, N. H. & H. R. Co., supra*).

No plan of reorganization may be submitted to the vote of creditors and stockholders by the Commission unless such plan has received the independent approval of the judge, and the judge must be satisfied as to the results of the submission to creditors and stockholders found by the Commission. A finding of the Commission that submission to any class of creditors or stockholders is not necessary is without force unless affirmed by the judge. The determination whether the rights of creditors and stockholders who refuse to accept the plan are adequately protected is left to the judge. Final confirmation of a plan is left to the judge.

Throughout the statute it is abundantly clear that a proceeding in bankruptcy, a judicial proceeding, is contemplated; and the adjudication and protection of private rights is at every point left to the court.

True, by the provisions of Section 77, Congress has delegated to the Commission primarily the duty of determining certain matters. Among these are the following: (1) the ratification of the appointment of trustees for the debtor [subsection (c) (1)]; (2) the fixing of maximum limits for expenses and fees to be paid by the debtor's estate [subsection (c) (2) and (12)]; (3) the determination of the value of any property of the debtor for any purpose under Section 77 if it shall be necessary to determine such value [subsection (e)]; and (4) whether the plan of reorganization will be compatible with the public interest [subsection (d)]. Only the third and fourth questions mentioned are in issue before this Court.

To the Commission primarily are referred issues affecting the public interest (not "determination of the extent and character of the capitalization"), but these issues also

affect private rights. As to private rights, the Commission's findings and conclusions are preliminary and advisory. Similarly, the court may deal in a preliminary way with questions affecting the public interest. In authorizing the abandonment or sale of lines or portions of lines under subsection (o), the Court makes a preliminary determination of public interest, subject to the subsequent approval of the Commission. Also, in paragraph (6) of subsection (c), during the administration, the judge may decree, after hearing, that would be "contrary to the public interest" for a lessor of the debtor to operate a leased line, in which case the Commission is given full authority in abandonment proceedings.

Cooperation and coordination are necessary for a successful reorganization, but this does not justify a refusal by the court to perform its duties.

The determination by the Commission, that the plan approved by it is compatible with the public interest, does not indicate that no other plan would be compatible with the public interest and does not require the Court to approve the plan certified by the Commission without a critical examination and determination of judicial questions affecting private rights. Another plan may be framed which will adequately protect private rights and be compatible with the public interest. Section 77 does not purport to make the findings of the Commission conclusive upon the Court.

The Commission's Determinations Are Not Binding on the District Court.

Even if we should concede that the determination, whether a plan of reorganization of the debtor railroad is compatible with the public interest, has been referred by Congress to the Commission exclusively, a finding of the Commission upon this question is subject to review by the District Court and upon this appeal if such a

finding is made arbitrarily or without support in the evidence, or if it results in the confiscation of private property rights.

St. Joseph Stock Yards Co. v. *United States,* 298 U. S. 38;
Baltimore & Ohio R. Co. v. *United States,* 298 U. S. 349;
Crowell v. *Benson,* 285 U. S. 22.

When the issue is whether the findings of the Commission result in the confiscation of private property rights, the Court is not bound to accept those findings even though supported by substantial evidence. Upon this issue the Court must weigh the evidence and determine the facts independently.

In *St. Joseph Stock Yards Co.* v. *United States,* 298 U. S. 38, this Court said (pp. 49-50, 52):

> "A preliminary question is presented by the contention that the District Court, in the presence of this issue [confiscation], failed to exercise its independent judgment upon the facts [citing cases]. The District Court thought that the question was still an open one under the Packers and Stockyards Act, and expressed the view that, even though the issue is one of confiscation, the Court is bound to accept the findings of the Secretary if they are supported by substantial evidence and that it is not within the judicial province to weigh the evidence and pass upon the issues of fact. The Government points out that, notwithstanding what was said by the court upon this point, the court carefully analyzed the evidence, made many specific findings of its own, and in addition adopted, with certain exceptions, the findings of the Secretary. * * * Hence, the Government says that the decree should be affirmed irrespective of possible error in the reasoning of the District Court. * * *
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> "* * * But to say that their findings of fact may be made conclusive where constitutional rights of liberty and property are involved, although the evidence clearly establishes that the findings are wrong and constitutional rights have been invaded, is to place those rights at the mercy of administrative officials and seriously to impair the security inherent in our judicial safeguards. * * * The principle applies when rights either of person or of property are protected by constitutional restrictions. Under our system there is no warrant for the view that the judicial power of a competent court can be circumscribed by any legislative arrangement designed to give effect to administrative action going beyond the limits of constitutional authority. This is the purport of the decisions above cited with respect to the exercise of an independent judicial judgment upon the facts where confiscation is alleged. The question under the Packers and Stockyards Act is not different from that arising under any other act, and we see no reason why those decisions should be overruled."

And in *Baltimore & Ohio R. Co.* v. *United States*, 298 U. S. 349, 368-369, the Court said:

> "* * * when he [the owner of private property] appropriately invokes the just compensation clause, he is entitled to a judicial determination of the amount. The due process clause assures a full hearing before the court or other tribunal empowered to perform the judicial function involved. That includes the right to introduce evidence and have judicial findings based upon it."

In *Crowell* v. *Benson*, 285 U. S. 22, where the Court even required a trial *de novo* on jurisdictional facts, the Court said (p. 60):

> "In cases brought to enforce constitutional rights, the judicial power of the United States necessarily extends to the independent determination of all questions, both of fact and law, necessary to the performance of that supreme function. The case of confiscation is illustrative, the ultimate conclusion almost invariably depending upon the decisions of

> questions of fact. This court has held the owner to be entitled to 'a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both law and facts.' *Ohio Valley Water Co.* v. *Ben Avon Borough, supra.* * * *"

Moreover, if the Commission in making an administrative determination has committed an error of law or foreclosed determination by the Court of questions of private rights, the error of the Commission must be corrected by the courts. The Court must make an independent determination of challenged questions of law which are involved in administrative determinations and, if necessary, must examine the entire record, including the evidence (*St. Joseph Stock Yards Co.* v. *United States*, 298 U. S. 38, at page 74). The Court's reversal of the Commission upon a question of law will be binding on the Commission but will not prevent it from enforcing the legislative policy committed to its charge, within the limits of the law as declared by the courts.

> *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134;
> *Federal Power Commission* v. *Pacific Co.*, 307 U. S. 156.

The powers of the district courts under Section 77 were discussed by Mr. Justice Frankfurter in *Palmer* v. *Massachusetts*, 308 U. S. 79, in considering whether the statute confers upon the district courts power to authorize the abandonment by the debtor's trustees of local passenger stations without securing the approval of state agencies. He stated that the provision of Section 77(a) giving the District Court "exclusive jurisdiction of the debtor and its property wherever located" and other general provisions, were doubtless sufficient "to confer upon the district courts power appropriate for adjusting

property rights in the railroad debtor's estate and, as to such rights, beyond that in ordinary bankruptcy proceedings." He stated further: "The judicial process in bankruptcy proceedings under § 77 is, as it were, brigaded with the administrative process of the Commission"; and "the authority of the court is intertwined with that of the Commission."

Mr. Justice Reed has stressed cooperation:

> "* * * The judicial functions of the bankruptcy court and the administrative functions of the Commission work cooperatively in reorganizations. * * *" (*Warren* v. *Palmer*, 310 U. S. 132, 138)

In these statements one finds no indication that the District Court in approving a plan of reorganization is merely reviewing determinations of the Commission.

Both Court and Commission Must Perform Their Functions.

Section 77 contemplates and requires cooperation and coordinated action by the Commission and the District Court in bringing about a reorganization. The Commission must perform its administrative and quasi-judicial functions. The extent of the Commission's jurisdiction and the scope of its powers in this proceeding are fixed by the statute, and Commission action in excess of the authority conferred by the statute is always subject to review and control by the courts (*Federal Radio Commission* v. *Nelson Bros. Bond & Mortgage Co.*, 289 U. S. 266). The Commission's violation of law and failure to proceed according to law are discussed elsewhere in this brief. At this point we urge that the District Court failed to perform its proper functions as a court of bankruptcy, and that such failure is contrary to law and vitiates and nullifies the whole proceeding (*Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106; *Gross* v. *Irving Trust Co.*, 289 U. S. 342).

Review of mere administrative orders distinguished

The petitioners would apply to this reorganization proceeding principles and rules applicable to the review of Commission action as to rates, service regulations and similar administrative matters. In rate making, service regulation and the like, the Commission is a legislative or policy making body and its determinations and conclusions are binding if they are within the power conferred by Congress and are supported by evidence. This well settled proposition is supported by many decisions of this Court, including the following:

Terminal R. R. Assn. v. *United States*, 266 U. S. 17;
United States v. *Louisiana*, 290 U. S. 70;
United States v. *Illinois Central R. Co.*, 291 U. S. 457;
Atlanta, Birmingham & Coast R. Co. v. *United States*, 296 U. S. 33;
Manufacturers Ry. Co. v. *United States*, 246 U. S. 457.

When the Commission exercises the legislative or discretionary authority conferred by Congress, it is concerned "not so much with past situations as with future adjustments" and its determinations "are clothed with a high degree of finality." (SHARFMAN, *The Interstate Commerce Commission*, Vols. I, p. 7; II p. 357). Even under Section 20a of the Interstate Commerce Act, however, "The initiation of financial policies was left undisturbed in the hands of the carriers"; and the holding of hearings was optional (*Ibid.*, Vol. I, p. 191).

But the quasi-judicial acts of the Commission under Section 77 of the Bankruptcy Act deal directly with private rights. Hence, they do not possess "the high degree of

finality" of mere administrative determinations under the Interstate Commerce Act (REMINGTON ON BANKRUPTCY, Section 4326). It is for this reason that Section 77 has not taken over the statutory provisions which govern the review of regulatory action under the Interstate Commerce Act.

Review of the Commission's administrative orders is governed by the Urgent Deficiencies Act of October 22, 1913, and must be heard by a statutory three judge court (38 Stat. 208, 220, 28 U. S. C. A. § 47). Thereafter a direct appeal to the Supreme Court lies under Section 210 of the Judicial Code (28 U. S. C. A. § 47a). Appeals in bankruptcy, however are taken to the Circuit Court of Appeals and are governed by Section 24 of the Bankruptcy Act (11 U. S. C. A. § 47).

To label the actions of the Commission under Section 77 as "legislative" and in the "public interest" by pointing to its characteristic administrative functions under Section 20a of the Interstate Commerce Act (as has been attempted by the petitioners) is to conceal the Commission's quasi-judicial powers. "The fact is that the Interstate Commerce Commission is a legislative agency or an administrative agency or a quasi-judicial agency depending upon what part of its particular job one happens to be looking at. It has all three attributes simultaneously, or perhaps it would be more accurate to say that it exhibits them successively at different stages of its activity." (CUSHMAN, *The Constitutional Status of the Independent Regulatory Commissions*, 24 Cornell Law Quarterly 13, 47; see also *Ibid.*, 49).

While the District Court should not usurp "merely administrative functions" of the Commission, or substitute its judgment as to the wisdom or expediency of the Commission's administrative action, "the essence of judicial authority may not be curtailed" or "avoided" by the Court (*Interstate Commerce Commission* v. *Illinois Central R. Co.*, 215 U. S. 452, 470).

Summary

In approving the plan of reorganization the District Court doubted its power to pass upon the Commission's legislative determinations even if arbitrary or confiscatory. The Court completely overlooked the Commission's failure to act upon the basis of adequate data and make precise findings as to the basic factors of value and earning capacity (Point I, above). But the District Court also misinterpreted Section 77 and misconstrued its own functions and duties under that section and the law of the land. Even without an express statutory command, the Court must pass independent judgment upon challenged questions of law which are involved in or imbedded in administrative determinations of the Commission. Furthermore, by the express mandate of Section 77, the District Court must, as a condition of approving the plan of reorganization, be satisfied that the plan is fair and equitable and non-discriminatory, and that it gives due recognition to the rights of each class of creditors. Although the District Court may not control the Commission's determination whether the plan is "compatible with the public interest," except where the administrative action is capricious, arbitrary or confiscatory, or not supported by adequate data and findings, the Commission's determination of the public interest does not relieve the District Court of its duty under the statute to protect private rights (*Palmer* v. *Massachusetts*, 308 U. S. 79), and to determine whether the plan is fair and equitable and non-discriminatory as to bondholders, creditors and stockholders.

Congress did not, by the enactment of Section 77, "withdraw from the courts control over insolvent railroads and lodge it with the Interstate Commerce Commission." (*Palmer* v. *Massachusetts*, 308 U. S. 79, 87)

The District Court misinterpreted the statute and failed and refused to perform its judicial functions and thereby committed reversible errors of law.

POINT VII

Preferential treatment given the claim of the Reconstruction Finance Corporation under the Commission Plan is unsupported by necessary administrative or judicial findings and cannot be justified under the facts of this case.

In the Commission Plan it is provided that the Reconstruction Finance Corporation shall "receive for the secured notes of the debtor held by it, treatment equal to that accorded to the holders of the debtor's existing first-mortgage bonds" (R. 312). The Commission states that this preferential treatment of the government Corporation's secured claim is in consideration of the purchase by that Corporation of the $10,000,000 of new first mortgage four per cent bonds which are authorized for the purpose of raising the new money said to be needed to effect the reorganization, and in consideration of the value of the collateral securing the claim. No adequate finding of the value of the collateral is made.

Thus, the Commission Plan proposes that the Reconstruction Finance Corporation shall receive a substantial underwriting fee if it elects to take this $10,000,000 of new first lien bonds upon most favorable terms, without a finding as to the value of the new bonds and without reference to the marketability of the bonds at par. Its secured claim is to be advanced to a preferred position ahead of the secured claim of The Railroad Credit Corporation and far superior to the secured claim of A. C. James Co., which is to be funded only in part.

No provision is made for a public offering of the new first mortgage bonds though considerations of equity and law require such an offering and only in the event that no other purchaser is found should the government Corporation receive an underwriting fee. And yet the pro-

posed purchase of the new bonds by the Reconstruction Finance Corporation is subject to future approval thereof by the Commission.

The preferential treatment accorded to Reconstruction Finance Corporation, by funding its secured claim in full in the same kind of securities allocated to First Mortgage bondholders, while the secured claim of The Railroad Credit Corporation does not receive comparable treatment, and more than half of the secured claim of A. C. James Co. is cut off entirely, is a clear violation of the doctrine of priorities reaffirmed by this Court in *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106.

In *Case* v. *Los Angeles Lumber Products Co., supra,* this Court held that stockholders could not participate in the reorganization of an insolvent corporation upon the basis of the tenuous considerations alleged. The Court said (308 U. S. at p. 122):

> "In view of these considerations we believe that to accord 'the creditor his full right of priority against the corporate assets' where the debtor is insolvent, the stockholder's participation must be based on a contribution in money or in money's worth, reasonably equivalent in view of all the circumstances to the participation of the stockholder."

In the light of this principle the preferential treatment accorded to Reconstruction Finance Corporation cannot be justified. It is not "based on a contribution in money or in money's worth" which is reasonably equivalent to the reward conferred. No provision is made for a public offering of the new first mortgage bonds; no finding was made as to the fair value of these bonds or that they could not be sold at par or better.

Under the *Los Angeles* case the Court had ample power and discretion to make the needed finding as to "money's worth" and equivalency but there is no finding and no evidence that the value to the debtor's estate of the pro-

posed purchase of bonds by Reconstruction Finance Corporation is "reasonably equivalent in view of all the circumstances" to the value of the preference accorded to that Corporation.

Furthermore, the reward and preference which the Commission Plan contemplates for the Reconstruction Finance Corporation is in violation of the provisions of the Reconstruction Finance Corporation Act and Emergency Relief and Construction Act of 1932 (15 U. S. C. A., chap. 14, § 605), which authorizes loans to railroads engaged in interstate commerce only when such railroads are "unable to obtain funds through banking channels or from the general public." The section provides further:

> "* * * *Provided*, That no fee or commission shall be paid by any applicant for a loan under the provisions hereof in connection with any such application or any loan made or to be made hereunder, and the agreement to pay or payment of any such fee or commission shall be unlawful. * * *"

In addition to the above objections, it is now obvious that since the trustees of the debtor's properties now hold cash in an amount in excess of the total amount due on the Trustees' Certificates outstanding (see brief of Institutional Bondholders, p. 110), and this cash holding is rapidly increasing, it is at least doubtful that there is need for the issue of the proposed new first mortgage bonds in that amount to furnish new money "needed" for the purposes of the reorganization.

The preference is unfair, inequitable, discriminatory and contrary to law.

POINT VIII

The General and Refunding Mortgage is a first lien upon assets of the debtor sufficient in value to cover fully the claims of the three secured creditors, including this respondent.

The unfair and discriminatory treatment of A. C. James Co. and The Railroad Credit Corporation in relation to First Mortgage bondholders and Reconstruction Finance Corporation results principally from the Commission's drastic limitation upon capitalization and its failure to recognize and give legal effect in the plan of reorganization to the value of the debtor's property. The value of the property of the debtor on the basis of "earning power" and other relevant factors, we contend, is more than sufficient to provide fully for the claims of all secured creditors.

This unfair and discriminatory treatment also results from erroneous determinations of the Commission and Court as to the priority and coverage of the debtor's General and Refunding Mortgage. A. C. James Co. contends that the assets of the debtor upon which the General and Refunding Mortgage constitutes a prior lien, when taken with the assets upon which such mortgage constitutes a lien subject only to the First Mortgage of the debtor, are sufficient to cover fully the secured claims of Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Co., and hence, that all three of these secured creditors should receive treatment as favorable as that accorded to First Mortgage bondholders.

In support of its contention as to the coverage and priority of the debtor's General and Refunding Mortgage and the adequacy of the security held by it thereunder, A. C. James Co. adopts and relies upon the brief and argument submitted on behalf of the Irving Trust Company of New York, Trustee under the debtor's General and Refunding Mortgage.

IN CONCLUSION

At pages 4 to 9 of this brief there are set forth some of the reasons why it is desirable that this Court, in the interests of substantial justice, fully consider and definitely dispose of the broad issues as to the construction of Section 77 of the Bankruptcy Act which arise in this proceeding.

To this respondent it seems entirely clear, on the record before this Court, that the Circuit Court of Appeals for the Ninth Circuit correctly decided the issues which it considered, and should be affirmed. There are, however, weighty considerations, both of private interest and of public interest, which render it desirable, and almost essential in the interests of substantial justice, that this Court at this time consider broadly the construction of Section 77 of the Bankruptcy Act in its application to the facts before it in this proceeding.

Section 77 has by no means accomplished, in this proceeding or in other similar proceedings, the objectives sought by Congress. It has not, in practical operation, facilitated and speeded up the reorganization of those railroads which found themselves unable to meet their fixed charges, as a result of the enormous shrinkage in traffic which followed the 1929 collapse. It has not proved itself to be better machinery for reorganization than the old equity proceedings.

This failure to accomplish the legislative purposes is not due to any inherent defect in Section 77. The difficulties in administering Section 77 have clearly resulted from an attempted administrative distortion of the clear language of the statute. An unrealistic and doctrinaire distortion of the statute has resulted from an attempt to read into the statute economic and political theories which were not within the contemplation of Congress and have no practical justification. Only such a distortion of the language

of Section 77 can explain (but not justify) the result reached in this proceeding, where the Commission's theory led it to confiscate the larger part of the claim of a secured creditor (this respondent) without any such finding of the value of the debtor's property as would justify such confiscation.

The errors which the Circuit Court of Appeals found in the proceedings below were due to basic errors in the construction of Section 77 of the Bankruptcy Act. These errors were in no sense due to an inadvertent administration of the statute; they root back into a basic misconstruction of the legislative mandate which was embodied in Section 77.

Only if the statute is given finality at this time by a clear and comprehensive construction of the legislative intent embodied in Section 77 of the Bankruptcy Act, and its appropriate application to this proceeding, can the substantial interests of the parties to this proceeding be protected and the public interest conserved.

WHEREFORE, this respondent prays this Court that it dispose of all substantial issues raised before it in this proceeding, and, on the basis of its construction of Section 77, and its disposition of the substantial issues herein raised, that it affirm the decision of the Circuit Court of Appeals for the Ninth Circuit here under review.

Respectfully submitted,

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October 3, 1942.

APPENDIX.

Section 77 of the Bankruptcy Act (47 Stat. 1474 as amended by 49 Stat. 911, 49 Stat. 1969 and 53 Stat. 1406; 11 U. S. C. A. §205).

SEC. 77. REORGANIZATION OF RAILROADS ENGAGED IN INTERSTATE COMMERCE.—(a) Any railroad corporation may file a petition stating that it is insolvent or unable to meet its debts as they mature and that it desires to effect a plan of reorganization. The petition shall be filed with the court in whose territorial jurisdiction such corporation, during the preceding six months or the greater portion thereof, has had its principal executive or operating office, and a copy of the petition shall at the same time be filed with the Interstate Commerce Commission (hereinafter called the "Commission"): *Provided,* That when any railroad, although engaged in interstate commerce, lies wholly within one State, such proceedings shall be brought in the Federal district court of the district in which its principal operating office in such State during the preceding six months or the greater portion thereof has been located. The petition shall be accompanied by payment to the clerk of a filing fee of $100, which shall be in addition to the fees required to be collected by the clerk under other sections of this Act. Upon the filing of such a petition, the judge shall enter an order either approving it as properly filed under this section, if satisfied that such petition complies with this section and has been filed in good faith, or dismissing it, if he is not so satisfied. If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with

this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose. Process of the court shall extend to and be valid when served in any judicial district. The Supreme Court of the United States shall promulgate rules relating to the service of process outside of the district in which the proceeding is pending, and any other rules which it may deem advisable in order to aid district courts and circuit courts of appeal in exercising the jurisdiction herein conferred upon them. The railroad corporation shall be referred to in the proceedings as a "debtor." Any railroad corporation the majority of the capital stock of which having power to vote for the election of directors is owned, either directly or indirectly through an intervening medium, by any railroad corporation filing a petition as a debtor may file, with the court in which such other debtor has filed such a petition, and in the same proceeding, a petition, a copy of which shall also be filed at the same time with the Commission, stating that it is insolvent or unable to meet its debts as they mature, and that it desires to effect a reorganization in connection with, or as a part of the plan of reorganization of such other debtor; and upon the filing of such petition, the judge shall enter an order either approving it as properly filed under this section, if satisfied that such petition complies with this section and has been filed in good faith, or dismissing it if not so satisfied, and thereupon such court, if it approves such petition, shall have the same jurisdiction with respect to such debtor, its property and its creditors and stockholders, as the court has with respect to such other debtor. Creditors of any railroad corporation, having claims aggregating not less than 5 per centum of all the indebtedness of such corporation as shown in the latest annual report which it has filed with the Commission at the time when the petition is filed, may, if such corporation has not filed a petition under this sec-

tion, file with the court in which such corporation might file a petition under this section, a petition stating that such corporation is insolvent or unable to meet its debts as they mature and that such creditors have claims aggregating not less than 5 per centum of all such indebtedness of such corporation and propose that it shall effect a reorganization; copies of such petition shall be filed at the same time with the Commission and served upon such corporation. Such corporation shall, within ten days after such service, answer such petition. If such answer shall admit the jurisdiction of the court and the material allegations of the petition, the judge shall enter an order approving the petition as properly filed if satisfied that it complies with this section and has been filed in good faith, or dismissing it, if not so satisfied. If such answer shall deny either the jurisdiction of the court or any material allegation of the petition the judge shall summarily determine the issues presented by the pleadings without the intervention of a jury and if he shall find that the material allegations are sustained by the proofs and that the petition complies with this section and has been filed in good faith, the judge shall enter an order approving the petition; otherwise he shall dismiss the petition. If any such petition shall be so approved, the proceedings thereon shall continue with like effect as if the railroad corporation had itself filed a petition under this section. In case any petition shall be dismissed, neither the petition nor the answer of a debtor shall constitute an act of bankruptcy or an admission of insolvency or of inability to meet maturing obligations or be admissible in evidence, without the debtor's consent, in any proceedings then or thereafter pending or commenced under this Act or in any State or Federal court. If, in any case in which the issues have not already been tried under the provisions of this subdivision, any of the creditors shall, prior to the hearing provided for in paragraph (1) of subsection (c) of this section, appear

and controvert the facts alleged in the petition, the judge shall determine, as soon as may be, the issues presented by the pleadings, without the intervention of a jury, and, unless the material allegations of the petition are sustained by the proofs, shall dismiss the petition.

(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien

at not less than a fair upset price, the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of defaults, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the charter of the debtor, and/or the issuance of securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.

The adoption of an executory contract or unexpired lease by the trustee or trustees of a debtor shall not preclude a rejection of such contract or lease in a plan of reorganization approved hereunder, and any claim resulting from such rejection shall not have priority over any other claims against the debtor, because such contract or lease had been previously adopted. The term "securities" shall include evidences of indebtedness either secured or unsecured, bonds, stock, certificates of beneficial interest therein, certificates of beneficial interest in property, options, and warrants to receive, or to subscribe for, securities. The term "stockholders" shall include the holders of voting-trust certificates. The term "creditors" shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act, including the holder of a claim under a contract executory in whole or in part including an unexpired lease.

The term "claims" includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character. For all purposes of this section unsecured claims, which would have been entitled to priority if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition, shall be entitled to such priority and the holders of such claims shall be treated as a separate class or classes of creditors. In case an executory contract or unexpired lease of property shall be rejected, or shall not have been adopted by a trustee appointed under this section, or shall have been rejected by a receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, or shall be rejected by any plan, any person injured by such nonadoption or rejection shall for all purposes of this section be deemed to be a creditor of the debtor to the extent of the actual damage or injury determined in accordance with principles obtaining in equity proceedings. The provisions of section 60 of this Act shall apply to a proceeding under this section. For all purposes of this section any creditor or stockholder may act in person or by an attorney at law or by a duly authorized agent or committee subject to the provisions of subsection (p) hereof. The running of all statutes of limitation shall be suspended during the pendency of a proceeding under this section.

(c) After approving the petition:

(1) The judge shall forthwith (and in pending proceedings immediately upon the effective date of this amendatory section) require the debtor to give such notice as the order may direct to the mortgage trustees, creditors and stockholders, and to cause publication thereof for such period and in such newspapers as the judge may direct, of a hearing to be held not later than thirty days

after the date of such order, at which hearing or any adjournment thereof the judge shall appoint one or more trustees of the debtor's property. Such appointments shall become effective upon ratification thereof by the Commission without a hearing, unless the Commission shall deem a hearing necessary. Where a trustee is appointed who within one year prior thereto has been an officer, director, or employee of the debtor corporation, any subsidiary corporation, or any holding company connected therewith, the judge, subject to ratification by the Commission as herein provided, shall appoint another trustee or trustees who shall not have had any such affiliations: *Provided*, That the appointment of such additional trustee or trustees shall not be required for a debtor the annual operating revenues of which were less than $1,000,000 for the previous calendar year.

(2) The judge shall fix the amount of the bond of every trustee. He may thereafter terminate any such appointments on cause shown, and may in that event and in the event of a vacancy from any other cause, in the manner and within the qualifications herein provided for the appointment of trustees, appoint a substitute trustee or trustees, and in the same manner and within the same qualifications may appoint an additional trustee, and shall fix the amount of the bond of every such substitute or additional trustee or trustees. The judge shall in his discretion confirm the appointment of such legal counsel for the trustees as they shall select, with power of removal. The trustee or trustees and their counsel shall receive only such compensation from the estate of the debtor as the judge may from time to time allow within such maximum limits as may be approved by the Commission as reasonable. The trustee or trustees so appointed, upon filing such bond, shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all of the powers of a trustee

appointed pursuant to section 44 of this Act or any other section of this Act, and, to the extent not inconsistent with this section, if authorized by the judge, the powers of a receiver in an equity proceeding, and, subject to the control of the judge and the jurisdiction of the Commission as provided by the Interstate Commerce Act as now or hereafter amended, the power to operate the business of the debtor. Prior to the appointment of a trustee, the debtor on behalf of the court shall continue in the possession of the property and shall operate the business thereof during such period, and shall have all the title to the property and shall exercise all power consistent with the provisions of this section, subject at all times to the control of the judge, and to such limitations, restrictions, terms, and conditions as he may from time to time impose and prescribe.

(3) The judge may, upon not less than fifteen days' notice published in such manner and in such newspapers as the judge may in his discretion determine, which notice so determined shall be sufficient, for cause shown, and with the approval of the Commission, in accordance with section 20 (a) of the Interstate Commerce Act, as now or hereafter amended, authorize the trustee or trustees to issue certificates for cash, property, or other consideration approved by the judge, for such lawful purposes and upon such terms and conditions and with such security and such priority in payments over existing obligations, secured or unsecured, or receivership charges, as might in an equity receivership be lawful.

(4) The judge shall require the officers of the debtor or the trustee or trustees, at such time or times as the judge may direct, and in lieu of the schedules required by section 7 of this Act, to file with the court such schedules and submit such other information as may be necessary to disclose the conduct of the debtor's affairs and the fair-

ness of any proposed plan; and shall direct the officers of the debtor, or the trustee or trustees, within such time as the judge shall set, to prepare and file with the court a list of all known bondholders and creditors of the debtor, and the amounts and character of their debts, claims, and securities, and the last known post-office address or place of business of each bondholder and creditor, and a list of all known stockholders of the debtor, with the last known post-office address or place of business of each, which lists the judge may require to be brought down to date at any time. The contents of such lists shall not constitute admissions by the debtor or the trustees in a proceeding under this section or otherwise.

(5) [Securing information as to holders of securities.]

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(6) [Rejection of leases.]

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(7) The judge shall promptly determine and fix a reasonable time within which the claims of creditors may be filed or evidenced and after which no claim not so filed or evidenced may participate except on order for cause shown; the manner in which such claims may be filed or evidenced and allowed, and for the purposes of the plan and its acceptance, after notice and hearing, the division of creditors and stockholders into classes according to the nature of their respective claims and interests. Such division shall not provide for separate classification unless there be substantial differences in priorities, claims, or interests. The trustee or trustees under any mortgage, deed of trust, or indenture outstanding against the property may, within the time prescribed, file a verified claim in behalf of all bonds or securities outstanding under such mortgage, deed of trust, or indenture, in which event it shall be unnecessary for the holders of such bonds or

securities to file claims in their own behalf, but nothing herein shall constitute such trustee or trustees the representative or representatives of such holders for the purpose of accepting or rejecting any plan of reorganization.

(8) The judge shall cause reasonable notice of the period in which claims may be filed, of hearings on application for the dismissal of the proceedings, or for the final allowance of fees or expenses to be given creditors and stockholders by publication or otherwise.

(9) [Reports of fraud, etc.]

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(10) The judge may direct the debtor or the trustee or trustees to keep such records and accounts, in addition to the accounts prescribed by the Commission, as will permit of such a segregation and allocation, as the necessities of the case may require, of the earnings and expenses between and to the divisions and parts of the railroad or other property of the debtor which are separately subject to the liens of the various mortgages or deeds of trust, or are separately subject to lease, and may refer to the Commission for its recommendations after hearings thereon if the parties shall so request and/or the Commission determine necessary or desirable, as to the method or formula by which such segregation and allocation shall be made; and thereafter such segregation and allocation may be made at the expense of the debtor's estate.

(11) The Commission may direct such of its agencies as it may designate to file in the proceedings before the Commission a report, and additional or supplemental reports at such time or times as the Commission shall designate, of such data with reference to the property, business, earnings, and corporate organization of the debtor and such other facts as the Commission, after hearing if it deems necessary, shall determine to be necessary or help-

ful information for the purposes of the preparation of reorganization plans, and for the purpose of aiding in determining the method or formula of allocating earnings permitted by subdivision (10) of this subsection (c). Such report or reports shall be prima facie evidence of the facts therein stated in any proceeding under this section. The actual cost of preparing said report or reports shall be certified by the Commission and shall be borne by the debtor's estate.

(12) [Allowances.]

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(13) The judge may on his own motion or at the request of the Commission refer any matters for consideration and report, either generally or upon specified issues, to one of several special masters who shall have been previously designated to act as special masters in any proceedings under this section by order of any circuit court of appeals and may allow such master a reasonable compensation for his services and actual and reasonable expenses. The circuit court of appeals of each circuit shall designate three or more members of the bar as such special masters whom they deem qualified for such services, and shall from time to time revise such designations by changing the persons designated or their number, as the public interest may require: *Provided, however,* That there shall always be three of such special masters qualified for appointment in each circuit who shall hear any matter referred to them under this section by a judge of any district court. The debtor, any creditor or stockholder, or the duly authorized committee, attorney or agent of either or the trustee or trustees of any mortgage, deed of trust or indenture pursuant to which securities of the debtor are outstanding, shall have the right to be heard on all questions arising in the proceedings, and, upon petition therefor and cause shown, any such person or any

other interested party may be permitted to intervene. The judge may, after hearing, make reasonable rules defining the matters upon which notice shall be given to other than interveners and the manner of giving such notice.

(d) The debtor, after a petition is filed as provided in subsection (a), shall file a plan of reorganization within six months of the entry of the order by the judge approving the petition as properly filed, or if heretofore approved, then within six months of the effective date of this Act, and not thereafter unless such time is extended by the judge from time to time for cause shown, no single extension at any one time to be for more than six months. Such plan shall also be filed with the Commission at the same time. Such plans may likewise be filed at any time before, or with the consent of the Commission during, the hearings hereinafter provided for, by the trustee or trustees, or by or on behalf of the creditors being not less than 10 per centum in amount of any class of creditors, or by or on behalf of any class of stockholders being not less than 10 per centum in amount of any such class, or with the consent of the Commission by any party in interest. After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

The Commission may thereafter, upon petition for good cause shown filed within sixty days of the date of its order, and upon further hearings if the Commission shall deem necessary, in a supplemental report and order modify any plan which it has approved, stating the reasons for such modification. The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan. No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court.

(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far

as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: Provided, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time

of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further,* That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States, or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is

required under this subsection holding, more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law; *Provided*, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e): Provided further, That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interests in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance, certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: *Provided further*, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the plan, he shall enter an order

and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

(f) Upon confirmation by the judge, the provisions of the plan and of the order of confirmation shall, subject to the right of judicial review, be binding upon the debtor, all stockholders thereof, including those who have not, as well as those who have, accepted it, and all creditors secured or unsecured, whether or not adversely affected by the plan, and whether or not their claims shall have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have accepted

it. Upon confirmation of the plan, the debtor and any other corporation or corporations organized or to be organized for the purpose of carrying out the plan, shall have full power and authority to, and shall put into effect and carry out the plan and the orders of the judge relative thereto, under and subject to the supervision and the control of the judge, the laws of any State or the decision or order of any State authority to the contrary notwithstanding. The property dealt with by the plan, when transferred and conveyed to the debtor or to the other corporation or corporations provided for by the plan, or when retained by the debtor pursuant to the plan, shall be free and clear of all claims of the debtor, its stockholders and creditors, and the debtor shall be discharged from its debts and liabilities, except such as may consistently with the provisions of the plan be reserved in the order confirming the plan or directing such transfer and conveyance or retention; and the judge may require the trustee or trustees appointed hereunder, the debtor, any mortgagee, the trustee of any obligation of the debtor, and all other proper and necessary parties, to make any such transfer or conveyance, and may require the debtor to join in any such transfer or conveyance made by the trustee or trustees. Upon the termination of the proceedings a final decree shall be entered discharging the trustee or trustees, and making such provisions as may be equitable, by way of injunction or otherwise, and closing the case. Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan and not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended. The provisions of title I and of section 5 of the Securities Act of 1933, as amended,

shall not apply to the issuance, sale, or exchange of any of the following securities, which securities and transactions therein shall, for the purposes of said Securities Act, be treated as if they were specifically mentioned in sections 3 and 4 of the said Securities Act, respectively: (1) All securities issued pursuant to any plan of reorganization confirmed by the judge in accordance with the provisions of this section; (2) all securities issued pursuant to such plan for the purpose of raising money for working capital and other purposes of such plan; (3) all securities issued by the debtor or by the trustee or trustees pursuant to subdivision (*e*), clause (3) of this section; (4) all certificates of deposit representing securities of, or claims against, the debtor, with the exception of such certificates of deposit as are issued by committees not subject to subsection (p) hereof. The provisions of subdivision (a) of section (14) of the Securities Exchange Act of 1934 shall not be applicable with respect to any action or matter which is within the provisions of subsection (p) hereof.

(g) If in the light of all the existing circumstances there is undue delay in a reasonably expeditious reorganization of the debtor, the judge, in his discretion, shall, on motion of any party in interest or on his own motion, after hearing and after consideration of the recommendation of the Commission, dismiss the proceedings. Upon the filing of such an order of dismissal, all right, title, or interest of the trustee or trustees shall vest by operation of law in the debtor unless otherwise provided by such order.

(h) [Revenue acts inapplicable to issuance, etc. of securities.]

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(i) [Transfer of title between receivers and trustees or to debtor.]

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(j) [Restraining or staying commencement or continuation of proceedings against debtor; removal of causes; owners' rights to equipment leased or conditionally sold unaffected.]

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(k) [Certified copy of order confirming plan or directing conveyance of property as evidence.]

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(l) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed.

(m) The term "railroad corporation" as used in this amendatory section means any common carrier by railroad engaged in the transportation of persons or property in interstate commerce, except a street, a suburban, or interurban electric railway which is not operated as a part of a general railroad system of transportation or which does not derive more than 50 per centum of its operating revenues from the transportation of freight in standard steam railroad freight equipment. Wherever used in this section the term "person" shall include an individual, corporation, partnership, association, joint-stock company, unincorporated organization, or a government or political subdivision thereof.

(n) [Claims of employees for personal injuries and claims of sureties as preferred claims; change in wages or working conditions regulated; moving shops, etc. regulated.]

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(o) The trustee or trustees, from time to time, shall determine what lines or portions of lines of railroad and what other property of the debtor, if any, should be abandoned or sold during the pendency of the proceedings in the interest of the debtor's estate and of ultimate reorganization but without unduly or adversely affecting the public interest, and shall present to the judge petitions, in which other parties in interest may join, for authority to abandon or to sell any such property; and upon order of the judge made after a hearing pursuant to such reasonable notice by publication or otherwise as the judge may direct to parties in interest, authorizing any such abandonment or sale, but only with the approval and authorization of the Commission when required by the Interstate Commerce Act as amended February 28, 1920, or as it may be hereafter amended, the trustee or trustees shall take all steps and carry out all proceedings necessary for the consummation of any such abandonment or sale in accordance with the order of the judge. Any such order of the judge shall be a final order for the purposes of appeal. The judge may order and decree any sale of property, whether or not incident to an abandonment, under this subsection at public or private sale and subject to or free from liens. The proceeds derived from any such sales shall be received by the trustee or trustees subject, in case the property was sold free from lien, to any liens thereon at the time of sale, and shall be applied or disposed of in such manner as the judge by further order shall direct. The expense of such sale shall be borne in such manner as the judge may determine to be equitable. The judge may order the trustee or trustees of the debtor to deposit such proceeds with any mortgage trustee entitled thereto, to be applied in payment of all or part of such mortgage.

(p) It shall be unlawful for any person, during the pendency of proceedings under this section or of receiver-

ship proceedings against a railroad corporation in any State or Federal court, (a) to solicit, or permit the use of his name to solicit, from any creditor or shareholder of any railroad corporation by or against whom such proceedings have been instituted, any proxy or authorization to represent any such creditor or shareholder in such proceedings or in any matters relating to such proceedings, or to vote on his behalf for or against, or to consent to or reject, any plan of reorganization proposed in connection with such proceedings; or (b) to use, employ, or act under or pursuant to any such proxy or authorization from any such creditor or shareholder which has been solicited or obtained prior to the institution of such proceedings; or (c) to solicit the deposit by any such creditor, or shareholder, of his claim against or interest in such railroad corporation, or any instrument evidencing the same, under any agreement authorizing anyone other than such depositor to represent such depositor in such proceedings or in any matters relating to such proceedings, including any matters relating to the deposited security or claim; or to vote such claim or interest or to consent to or reject any such plan of reorganization; or (d) to use, employ, or act under or pursuant to any such agreement with such depositor which has been solicited or obtained prior to the institution of such proceedings; unless and until, upon proper application by any person proposing to make such solicitation or to use, employ, or act under or pursuant to such proxies, authorizations, or deposit agreements, and after consideration of the terms and conditions (including provisions governing the compensation and expenses to be received by the applicant, its agents and attorneys, for their services) upon which it is proposed to make such solicitation or to use, employ, or act under or pursuant to such proxies, authorizations, or deposit agreements, the Commission after hearing by order authorizes such solicitation, use, employment, or action: *Provided, however,*

That nothing contained in this section shall be applicable to or construed to prohibit any person, when not part of an organized effort, from acting in his own interest, and not for the interest of any other, through a representative or otherwise, or from authorizing a representative to act for him in any of the foregoing matters, or to prohibit groups of not more than twenty-five bona fide holders of securities or claims or groups of mutual institutions from acting together for their own interests and not for others through representatives or otherwise or from authorizing representatives of such groups to act for them in respect to any of the foregoing matters. The Commission shall make such order only if it finds that the terms and conditions upon which such solicitation, use, employment or action is proposed are reasonable, fair, and in the public interest, and conform to such rules and regulations as the Commission may provide. The Commission shall have the power to make such rules and regulations respecting such solicitation, use, employment, or action and with respect to the terms and the provisions of such proxies, authorizations, and deposit agreements, and with respect to such other matters in connection with the administration of this subsection as it deems necessary or desirable to promote the public interest, and to insure proper practices in the representation of creditors and stockholders through the use of such proxies, authorizations, or deposit agreements and in the solicitation thereof. It shall be unlawful for any person to solicit any such proxy, authorization, or the deposit of any such claim or interest or to use, employ, or act under or pursuant to any such proxy, authorization, or deposit agreement which has been solicited or obtained prior to the institution of such proceedings in violation of the rules and regulations so prescribed.

Every application for authority shall be made in such form and contain such matters as the Commission may

prescribe. Every such application shall be made under oath, signed by, or on behalf of, the applicant by a duly authorized agent having knowledge of the matters therein set forth. The Commission may modify any order authorizing such solicitation, use, employment, or action by a supplemental order, but no such modification shall invalidate action previously taken, or rights or obligations which have previously arisen, in conformity with the Commission's prior order or orders authorizing such solicitation, use, employment, or action.

The Commission may, in its discretion, make such investigations as it deems necessary to determine whether any person has violated or is about to violate any provision of this subsection (p) or any rule or regulation thereunder, and may require or permit any person to file with it a statement in writing, under oath, or otherwise as the Commission shall determine, as to all the facts and circumstances concerning the matter to be investigated. The Commission is authorized, in its discretion, to publish information concerning any such violations, and to investigate any such facts, conditions, practices, or matters as it may deem necessary or proper to aid in the enforcement of the provisions of this subsection (p), in the prescribing of rules and regulations thereunder, or in securing information to serve as a basis for recommending further legislation concerning the matters to which this subsection relates.

Any person who willfully violates any provision of this subsection, or any rule or regulation made thereunder the violation of which is made unlawful, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed hereunder or under any rule or regulation authorized hereby, which statement is false or misleading with respect to any material fact, shall be guilty of a mis-

demeanor, and on conviction in any United States court having jurisdiction, shall be punished by a fine of not less than $1,000 nor more than $10,000 or by imprisonment for not less than one year nor more than three years, or by both such fine and imprisonment, in the discretion of the court; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

The provisions of this subsection (p) shall not be applicable to any person or committee which has begun to solicit, obtain, or use proxies, authorizations, or deposit agreements prior to the effective date of this amendatory section in connection with proceedings under this section as in force prior to such effective date or receivership proceedings against a railroad then pending in any State or Federal court, unless such person or committee makes application to the Commission and receives authority to act as in this subsection provided, in which event the provisions of this subsection (p) shall be applicable to such person or committee, but such authorization shall not be upon terms which shall invalidate any action theretofore taken, or any rights or obligations which have theretofore arisen: *Provided*, That with respect to committees which are not subject to this subsection (p) the judge shall scrutinize and may disregard any limitations or provisions of any deposit agreements, committee, or other authorizations affecting any creditor or stockholder acting under this section and may enforce an accounting thereunder or restrain the exercise of any power which he finds to be unfair or not consistent with public policy, including the collection of unreasonable amounts for compensation and expenses.

(q) The provisions of section 12 of the Interstate Commerce Act, as amended March 2, 1889, February 10, 1891,

and February 28, 1920, shall be applicable to enable the Commission to perform its duties under this section and the provisions of such section shall apply to the debtor, any subsidiary or affiliated company, or any other person as herein defined.

(r) If any provision of this amendatory section, or the application thereof to any person or circumstances, is held invalid, the remainder of this amendatory section, or application of such provision to other persons or circumstances, shall not be affected thereby.

(s) Proceedings pending under this section (Act of March 3, 1933) on the effective date of this amendatory section shall continue under, and be governed by, the provisions of this amendatory section: *Provided*, That the enactment of this amendatory section shall not invalidate any action taken before its effective date pursuant to this section as it existed prior to the enactment of this amendatory section.

Report of the Interstate Commerce Commission, dated November 20, 1930 (Original Exhibit No. 47, R. 2323)

FINANCE DOCKET NO. 8548

WESTERN PACIFIC RAILROAD COMPANY
DEBENTURES

Submitted November 18, 1930. Decided November 20, 1930

Authority granted to issue $5,000,000 of 5 per cent gold debentures to be sold to the highest bidder at not less than par and accrued interest and the proceeds used in connection with the construction and acquisition of an extension to the applicant's railroad.
F. M. Angellotti for applicant.

REPORT OF THE COMMISSION

DIVISION 4, COMMISSIONERS MEYER, EASTMAN, AND MAHAFFIE

By DIVISION 4:

The Western Pacific Railroad Company, a common carrier by railroad engaged in interstate commerce, has duly applied for authority under section 20a of the interstate commerce act to issue $5,000,000 of 5 per cent gold debentures. No objection to the granting of the application has been presented to us.

The debentures are to be issued in connection with the financing of the applicant's Northern California extension. The construction by the applicant of approximately 112 miles of the extension and the construction and/or acquisition by it of approximately 36 miles jointly with the Great Northern Railway Company was authorized by our certificate and order of June 9, 1930, in *Great Northern Ry. Co. Construction*, 166 I. C. C. 3. A description of the extension is contained in our report in that proceeding;

The applicant has estimated the total cost to it of the construction and acquisition of the extension as $10,049,077. A portion of this amount will be derived from proceeds of $5,000,000 of its first-mortgage bonds authorized by our order of October 6, 1930, in *Western Pac. R. Co. Bonds,* 166 I. C. C. 536. The $5,000,000 of proposed debentures are to be issued to provide additional funds to be applied in payment of the cost of the extension.

The debentures will be issued under an indenture to be entered into between the applicant and the Chase National Bank of the City of New York, as trustee, under date of July 1, 1930. They may be issued in coupon or registered form in denominations of $500, $1,000, or any multiple thereof, the coupon debentures to be dated July 1, 1930, and the registered debentures to be dated as of July 1 or January 1 next preceding the date of issue, unless issued on either of those dates, in which event they are to be dated the date of issue. They will bear interest at the rate of 5 per cent per annum, payable semiannually on January 1 and July 1, and will mature January 1, 1950. All or any part of them will be redeemable at the election of the applicant on any interest date prior to maturity at par and accrued interest.

The indenture will provide that not to exceed 50 per cent of the cost of the extension shall be met by the issue of debentures and that the amount of debentures which may be issued and outstanding at any one time shall not exceed $5,000,000. In the indenture the applicant will covenant that, so long as any of the debentures shall be outstanding, neither the applicant nor any of its subsidiaries will mortgage or, except as required by the applicant's first mortgage dated June 26, 1916, pledge any property now owned or hereafter acquired, without calling for redemption all outstanding debentures, and making suitable provision for their payment. The covenant, however, does not restrict the issue of securities,

including the securing thereof by mortgage or pledge, by subsidiary companies so far as permitted by the first mortgage, or apply to purchase-money mortgages or pledges, or to the acquisition of property already subject to lien, the issue or reissue of bonds or other obligations issuable under any existing mortgage or deed of trust, the extension or refunding of bonds or other obligations issued thereunder, or the issue of equipment-trust obligations.

A written offer to purchase the debentures was made by the A. C. James Company, but as that company and the applicant to some extent have interlocking officers and directors the proposal has taken the form of an offer to bid at par for the debentures upon a public sale thereof. The applicant therefore proposes to offer the debentures at public sale to the highest bidder at not less than par and accrued interest.

We find that the proposed issue by the Western Pacific Railroad Company of $5,000,000 of 5 per cent gold debentures as aforesaid (*a*) is for a lawful object within its corporate purposes, and compatible with the public interest, which is necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (*b*) is reasonably necessary and appropriate for such purpose.

An appropriate order will be entered.

Report of the Interstate Commerce Commission, dated February 27, 1932 (Original Exhibit No. 53, R. 2341)

FINANCE DOCKET No. 9162

WESTERN PACIFIC RAILROAD COMPANY SECURITIES

Submitted February 27, 1932. Decided February 27, 1932

Authority granted to issue not exceeding $15,000,000 of general and refunding mortgage gold bonds, series A, and a promissory note or notes for not exceeding $5,000,000, said bonds or such part thereof as may be required, to be pledged as collateral security for a loan or loans and for the notes; and the notes to be exchanged at not less than par for an equal amount of outstanding 5 per cent debentures.

Frank M. Angellotti and *Carl Taylor* for applicant.

REPORT OF THE COMMISSION

DIVISION 4, COMMISSIONERS MEYER, EASTMAN, AND MAHAFFIE

By DIVISION 4:

The Western Pacific Railroad Company, a common carrier by railroad engaged in interstate commerce, by its application as amended, has duly applied for authority under section 20a of the interstate commerce act to issue not exceeding $15,000,000 of general and refunding mortgage gold bonds, series A, and a note or notes in the aggregate face amount of not exceeding $5,000,000, maturing not less than three years nor more than four years and 11 months from the date thereof, and to pledge

the bonds as collateral security for a certain loan or loans and for the note or notes. No objection to the granting of the application has been presented to us.

Our order of November 20, 1930, in *Western Pac. R. Co. Debentures,* 166 I. C. C. 720, authorized the applicant to issue not exceeding $5,000,000 of 5 per cent gold debentures in connection with the financing of its Northern California extension. By the indenture dated July 1, 1930, to the Chase National Bank of the City of New York, under which the debentures were issued, the applicant covenanted that, so long as any of the debentures were outstanding, neither it nor any of its subsidiaries, would mortgage or, except as required by the applicant's first mortgage dated June 26, 1916, pledge any property now owned or hereafter acquired, without calling for redemption all outstanding debentures and making suitable provision for their payment. The debentures were sold to the A. C. James Company. Under the terms of the sale it appears that that company has from time to time taken delivery of various amounts of the debentures so that as of February 8, 1932, the amount outstanding was $4,504,000, but is obligated to take the entire issue.

The applicant proposes to make a new mortgage on its properties and to do this must comply with the covenant mentioned. Therefore, it has arranged with the holder of the debentures to pay them by issuing to it a 5 per cent note or notes of an equal amount, to mature not less than 3 years nor more than 4 years 11 months from the date thereof, and to be secured by the pledge of bonds to be issued under the proposed mortgage. The note or notes will contain a provision for the acceleration of the maturity of the principal thereof in case of default under the first mortgage, or the proposed new mortgage, or any of the loans made to the applicant by the Reconstruction Finance Corporation or the Railroad Credit Corporation,

such provision for acceleration of principal to be in the form agreed upon by the applicant and the A. C. James Company. The applicant seeks authority to issue a note or notes in the maximum amount necessary to pay all the debentures which may be issued and outstanding under the authority heretofore granted.

The proposed new mortgage will be known as the applicant's general and refunding mortgage, will be dated as of January 1, 1932, and will be made to the Chase National Bank of the City of New York, as trustee. The mortgage will limit the amount of bonds that may be outstanding thereunder at any one time to $100,000,000, and will provide for the issue of bonds to refund the applicant's first-mortgage bonds issued under its first mortgage dated June 26, 1916, and the $5,000,000 of debentures issued under the indenture of July 1, 1930. The mortgage will also provide that bonds may be issued in series as determined by the board of directors, and under section 1 of article two $15,000,000 of general and refunding mortgage bonds of any series, one or more, may be authenticated and delivered without further action on the part of the applicant, except the filing with the trustee of (1) resolutions of the board of directors, requesting authentication and delivery of the bonds, and (2) an opinion of counsel. Pursuant to these provisions, the board of directors has determined that the initial series of general and refunding mortgage gold bonds in the total amount of $15,000,000 is to be designated series A.

The series A bonds may be issued either in coupon or registered form, coupon and registered bonds being interchangeable. Coupon bonds in denominations of $1,000 and $500 will be dated January 1, 1932, and registered bonds in the denomination of $1,000 or any multiple thereof will be dated the day of issue, if an interest date, or, if not, the last preceding interest date, and will bear interest

from the date thereof. The bonds of this series will be redeemable at the applicant's election either in whole or in part on any interest date at par and accrued interest, will bear interest at the rate of 5 per cent per annum, payable semiannually on January 1 and July 1, and will mature January 1, 1957.

The applicant has applied for a loan from the Reconstruction Finance Corporation to aid in temporarily financing its requirements and has also applied for a loan from the Railroad Credit Corporation to enable it to meet its fixed interest charges maturing on March 1, 1932. The applicant states that since the filing of these applications it has been advised that the Railroad Credit Corporation is without funds and that arrangements have been made between the two corporations whereby it is expected the Reconstruction Finance Corporation will loan to the applicant the amount applied for from the Railroad Credit Corporation, or so much thereof as may be approved.

In applying for the loans mentioned, the applicant offered to pledge as security for each of the loans such principal amount of the proposed general and refunding mortgage gold bonds, series A, as the corporation making the loan should require and we should approve. As part of its agreement to accept in payment for the outstanding debentures a 5 per cent note or notes of a like face amount, the holder of the debentures required that the applicant should pledge as security for the note or notes general and refunding mortgage bonds, such security to be of the same maturity, to bear the same rate of interest, and to be comparable in all respects with the security for the loan or loans. Accordingly, the applicant requests authority to pledge series A bonds as collateral for the note or notes on the same basis at which they are pledged for the loans.

There was not submitted with the application in support of the proposed bonds a report of uncapitalized ex-

penditures listed on Form A, as required by our order of February 19, 1927, respecting applications filed under section 20a of the act. Because of the urgency of the applicant's receiving the authority sought, we will not require that the statement of expenditures and supporting data be filed before acting upon the application, but our order to be entered herein will require the applicant to file the requisite report on Form A together with the supporting data within three months from the date of the order. In the absence of specific expenditures to support the proposed bonds, it will be necessary to consider the applicant's capital assets and capital liabilities as shown by its general balance sheet as of December 31, 1931, filed with the application.

The investment in road and equipment amounts to $138,404,243.38, and "accrued depreciation, equipment" is shown at $7,537,331.79. Miscellaneous physical property amounts to $1,816,929.57. The greater portion of this amount represents the cost of real estate in San Francisco, Oakland, and Oakland Moie, Calif., held for the development of terminal facilities and the relocation of the applicant's main line in the city of Oakland; an appreciable portion of the amount represents investment in track material leased to various companies and would be classifiable as working capital; the remainder consists mostly of improved and unimproved property adjacent to the right of way located at various points along the line. While we are without an analysis of the various items comprising the investment in miscellaneous physical property, it appears that most of the property is either being used for railroad purposes or is intended ultimately to be used for such purposes. For the purposes of this application the entire amount will be considered as part of working capital. The investments in affiliated companies aggregate $14,781,334.36. The capital stock, bonds, and notes of subsidiary companies owned by the applicant will be pledged under

the proposed general and refunding mortgage subject to their prior pledge, if so pledged, under the applicant's first mortgage. Included under investments in affiliated companies are the following: Subscriptions to capital stock of Western Pacific California Railroad $27,500, Railway Express Agency, Incorporated, capital stock $200, advances $9,600, total $37,300. The applicant does not claim that any of these items are capitalizable. Under investments in affiliated companies are also various amounts of advances to subsidiary companies aggregating $3,473,533.33. It appears that a portion of the advances was made for operating expenses and therefore would not be capitalizable. As to the remainder, the capitalization thereof by the issue of proposed bonds would be premature and should be postponed until the subsidiaries have issued and delivered to the applicant their securities in satisfaction of the advances and such securities have been or will be pledged under the proposed general and refunding mortgage. See *Stock of Baltimore & O. R. Co.*, 154 I. C. C. 258, 260.

Giving effect to the foregoing, capital assets would consist of the following:

Investment in road and equipment	$138,404,243.38	
Less "accrued depreciation — equipment"	7,537,331.79	
		$130,866,911.59
Investments in affiliated companies		11,270,501.43
Working capital:		
Cash	946,117.22	
Material and supplies	2,255,823.50	
Miscellaneous physical property	1,816,929.57	
		4,918,870.29
Total		147,056,283.31

The outstanding capital liabilities consisted of the following:

Common stock	$ 47,500,000
Preferred stock	28,300,000
First-mortgage 5 per cent gold bonds	47,940,100
5 per cent gold debentures	4,154,000
Equipment-trust certificates	4,925,000
Total	132,819,100

As has been indicated above, the amount of outstanding 5 per cent gold debentures had increased from $4,154,000, the amount shown in the balance sheet, to $4,504,000 on February 8, 1932, and it is probable that the entire authorized amount of $5,000,000 will ultimately be issued. The proposed issue of not exceeding $5,000,000 of promissory notes and the pledge as security therefor of proposed general and refunding mortgage bonds for the purpose of paying the outstanding debentures are in the nature of temporary financing, inasmuch as under the proposed general and refunding mortgage $5,000,000 of bonds issuable thereunder is reserved to refund a like amount of 5 per cent gold debentures. Therefore, for the purpose of this application and a comparison of capital assets and capital liabilities, the $4,154,000 of outstanding debentures should be considered as having been replaced by the issue of $5,000,000 of general and refunding mortgage bonds. This change would increase the total capital liabilities to $133,665,100, making the excess of capital assets over capital liabilities amount to $13,391,183.31. It has been intimated that $5,000,000 of the proposed $15,000,000 of general and refunding mortgage bonds will ultimately be issued to refund a like amount of outstanding debentures. Therefore, it appears that the remaining $10,000,000 of proposed bonds may be considered as being issuable against the excess of capital assets over capital liabilities in the amount shown above.

In *Western Pacific Ry. Co.*, 29 Rep. 239-279, we reported the value of the property of the applicant as of June 30, 1914, pursuant to section 19a of the act. We there found the value for rate-making purposes of property owned and used by the applicant to be $63,861,208, including $561,208 for working capital. In addition, there was a small amount of common-carrier property owned but not used, and the applicant held other property which we classified as noncarrier, including lands, structures, and rights in the public domain, for which we found a value of $4,469,003. As accurately as it could be determined, the original cost of all the applicant's property as of valuation date was found to be $72,555,963.87. The investment in road and equipment, including land, as stated in the applicant's books at that time, was $156,318,136.40. Subsequent to valuation date the applicant was reorganized and the investment in road and equipment as stated on its books was reduced to approximately $83,000,000. Since valuation date the applicant has reported net additions and betterments to its property to the end of 1930 costing $39,030,394. If this amount be added to the value formerly found for the applicant's property, exclusive of working capital but including property owned and classified as noncarrier, this sum is approximately $106,800,000.

We find that the proposed issue (1) of not exceeding $15,000,000 of general and refunding mortgage gold bonds, series A, and (2) of a note or notes in the aggregate face amount of not exceeding $5,000,000 by The Western Pacific Railroad Company as aforesaid (*a*) is for lawful objects within its corporate purposes, and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (*b*) is reasonably necessary and appropriate for such purposes.

An appropriate order will be entered.

Report of the Interstate Commerce Commission, dated March 24, 1932 (Original Exhibit No. 53, R. 2341)

FINANCE DOCKET NO. 9162

WESTERN PACIFIC RAILROAD COMPANY SECURITIES

Submitted March 18, 1932 *Decided March 24, 1932*

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1. Order of February 27, 1932, 180 I. C. C. 652, amended so as to permit the applicant to issue, substantially in the form submitted with the supplemental application a note or notes in the aggregate face amount of not exceeding $5,000,000, to pledge as collateral security therefor general and refunding mortgage gold bonds, series A, in the ratio of not exceeding $125, principal amount, of bonds to each $100, face amount, of notes, and to exchange the notes at not less than par for not exceeding $5,000,000 of the applicant's 5 per cent gold debentures.

2. Authority granted, upon the surrender and cancellation of a note for $4,504,000 to issue in exchange therefor a note or notes in an equal aggregate face amount, to be secured by the pledge of $5,630,000, principal amount, of the applicant's general and refunding mortgage gold bonds, series A, provided that the total amount of notes to be outstanding at any one time under authority of the original and supplemental orders shall not exceed $5,000,000, and that the total amount of bonds to be pledged as collateral security for the notes shall not exceed $6,250,000.

Carl Taylor for applicant.

SUPPLEMENTAL REPORT OF THE COMMISSION

DIVISION 4, COMMISSIONERS MEYER, EASTMAN, AND MAHAFFIE

By Division 4:

Our order of February 27, 1932, in this proceeding, 180 I. C. C. 652, authorized The Western Pacific Railroad Company, the applicant herein, to issue not exceeding $15,000,000 of general and refunding mortgage gold bonds, series A, and a promissory note or notes in the aggregate face amount of not exceeding $5,000,000, to pledge the bonds as collateral security for a loan or loans and for the notes, and to exchange the notes at not less than par for an equal amount of the applicant's outstanding 5 per cent gold debentures.

By a supplemental application filed herein on March 16, 1932, the applicant seeks an amendment of the order so as to permit it to pledge the general and refunding mortgage gold bonds, series A, as collateral for the notes at the ratio hereinafter stated and to exchange the promissory notes for not exceeding $5,000,000 of 5 per cent gold debentures. Authority is also sought to issue a new note or notes in the principal amount of $4,504,000 in exchange for, and upon the surrender and cancellation of, a note in a like amount issued March 1, 1932, under the authority heretofore granted. No objection to the granting of the supplemental application has been presented to us.

The order of February 27, 1932, authorizes the general and refunding mortgage bonds to be pledged for the promissory note or notes in the same ratio as that for a loan or loans from the Railroad Credit Corporation or the Reconstruction Finance Corporation. The applicant shows that subsequent to the entry of the order of February 27, 1932, the holder of the 5 per cent gold debentures consented to modify its previous agreement and to accept as collateral for the note issued in exchange for the debentures general and refunding mortgage bonds in the ratio of $125, principal amount, of bonds, for each $100, face amount, of the note. Authority is sought to pledge

at the ratio indicated not exceeding $6,250,000 of bonds as collateral for not exceeding $5,000,000 of promissory notes.

The report filed with and made a part of the order of February 27, 1932, indicated that as of February 8, 1932, the debentures outstanding amounted to $4,504,000, but it also indicated that the total amount that might eventually be issued and outstanding was $5,000,000, as authorized by our order of November 20, 1930, in *Western Pac. R. Co. Debentures*, 166 I. C. C. 720, and that authority was sought to issue a note or notes in the maximum amount necessary to pay all the debentures which might be issued and outstanding under that order. However, the order of February 27, 1932, provided that the $5,000,000 of notes therein authorized to be issued was to be exchanged at not less than par for an equal amount of the applicant's outstanding 5 per cent gold debentures, which then amounted to $4,504,000. As the applicant proposes to issue presently $347,000 additional debentures, and expects to issue other debentures up to the authorized limitation of $5,000,000, all of which will be exchanged for notes as aforesaid, it considers it desirable to have the order modified so as to indicate that the notes may be exchanged for a maximum of $5,000,000 of debentures.

At the date of the original order in this proceeding a form or specimen of the proposed notes had not been filed and the order required that within 10 days after the execution of the note or notes the applicant should file with us a specimen or copy thereof. The applicant has complied with that part of the order and has filed a copy of its note dated March 1, 1932, for $4,504,000, payable three years after date, to the A. C. James Company, or order. A copy of this note is also filed with the supplemental application. It bears interest at the rate of 5 per cent per annum, payable quarterly on April 1, July 1, October 1, and January 1, and is secured by the pledge of $5,630,000 of the applicant's general and refunding mortgage gold bonds, series A. The applicant agrees to deposit with

the payee such additional security as the payee may from time to time demand. Provisions are also made for selling or otherwise disposing of the collateral in the event of the nonperformance of certain covenants and agreements therein specified, and for the payee's transferring the note and the collateral therefor. Authority is sought to issue a new note or notes to replace the note already issued. Any authority herein granted is not to be construed as authorizing the applicant to pledge as collateral for the note or notes any additional securities issued or assumed by it without first obtaining our authorization under section 20a.

We find that the issue by The Western Pacific Railroad Company (1) of not exceeding $15,000,000 of general and refunding mortgage gold bonds, series A, and of a note or notes in the aggregate face amount of not exceeding $5,000,000, as heretofore authorized, such an amount of the bonds as may be required, not exceeding $6,250,000, principal amount, to be pledged as collateral security for the note or notes at the ratio of not exceeding $125, principal amount, of bonds to each $100, face amount, of notes, and the note or notes to be substantially in the form submitted with the supplemental application, and (2) of a note or notes in the face amount of not exceeding $4,504,000 in exchange for a note for a like amount issued under authority of our order of February 27, 1932, herein, the new note to be substantially in the form submitted with the supplemental application and to be secured by the pledge of not exceeding $5,630,000 of the bonds to be pledged as collateral for notes authorized by that order, (*a*) is for lawful objects within its corporate purposes, and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (*b*) is reasonably necessary and appropriate for such purposes.

An appropriate supplemental order will be entered.

Report of the Interstate Commerce Commission, dated December 9, 1932 (Original Exhibit No. 92, R. 2458)

FINANCE DOCKET NO. 9572

WESTERN PACIFIC RAILROAD COMPANY BONDS

Submitted November 17, 1932. Decided December 9, 1932

1. Authority granted to issue not exceeding $4,000,000 of general and refunding mortgage gold bonds, series B, and to pledge applicant's equity therein, subject to their pledge to the Reconstruction Finance Corporation as collateral security for a note issued to the Railroad Credit Corporation amounting to $1,303,000, or any extension or renewal thereof. Condition prescribed.

2. That part of the application which seeks authority to pledge said bonds to the Reconstruction Finance Corporation dismissed.

Carl Taylor and *Rollin Browne* for applicant.

REPORT OF THE COMMISSION

DIVISION 4, COMMISSIONERS MEYER, EASTMAN, AND MAHAFFIE

BY DIVISION 4:

The Western Pacific Railroad Company, on August 5, 1932, applied for authority (1) to issue not exceeding $5,000,000 of general and refunding mortgage gold bonds, Series B, (2) to pledge them, or such amount thereof as we may authorize, to the Reconstruction Finance Corporation as collateral security for applicant's note dated June 29, 1932, for $734,584 payable to that corporation, or order, or for any extension or renewal thereof, and for

the payment of any other liability or liabilities of the applicant to the Finance Corporation, including a note dated March 1, 1932, for $799,000, and (3) to pledge all right, title, and interest in and to all of the series B bonds which may be pledged with the Finance Corporation, subject to the lien thereon of that corporation, to the Railroad Credit Corporation to secure the payment of applicant's note dated June 29, 1932, for $1,303,000, payable to the Credit Corporation, or order, or any extension or renewal thereof, as well as for the payment of any other liability or liabilities of the applicant to the Credit Corporation due or to become due or which may hereafter be contracted or existing, and as collateral for the payment of any and all indebtedness of the applicant to the Credit Corporation whether or not represented by a note or notes or in any manner secured and at any time or times incurred or to be incurred under the marshaling and distributing plan, 1934. No objection to the application has been offered.

The proposed bonds will be issued under and pursuant to the general and refunding mortgage dated January 1, 1932, made by the applicant to the Chase National Bank of the City of New York, trustee, and in accordance with the provisions of that mortgage a new series of bonds has been created to be designated as series B. The bonds of this series may be issued either in coupon or registered form, coupon and registered bonds being interchangeable. Coupon bonds in denominations of $1,000 and $500 will be dated July 1, 1932, and registered bonds in the denomination of $1,000, or any multiple thereof, will be dated the date of issue if an interest date, or, if not, the last preceding interest date, and will bear interest from the date thereof. The bonds of this series will be redeemable at the applicant's election either in whole or in part on any interest date at par and accrued interest, will bear interest at the rate of 5 per cent per annum, payable semi-annually on January 1 and July 1, and will mature January 1, 1957.

As part of the basis for the proposed issue of series B bonds, the applicant submits expenditures made during the period August 1, 1930, to May 31, 1932, for constructing its Northern California extension, in the amount of $10,183,641.90, of which $5,000,000 was capitalized by the issue of a like amount of first-mortgage gold bonds authorized to be issued by our order of October 6, 1930, in *Western Pac. R. Co. Bonds*, 166 I. C. C. 536, leaving $5,183,641.90 of expenditures to support the proposed bonds.

In *Western Pac. R. Co. Securities*, 180 I. C. C. 652, it was stated that the applicant had not submitted with the application filed in that proceeding a report of uncapitalized expenditures listed on form A, as required by our order of February 19, 1927, respecting applications filed under section 20a of the interstate commerce act and the order entered therein required the applicant to file such a report within three months from the date of the order. Pursuant to this requirement the applicant has filed the necessary form A purporting to show that during the period July 14, 1916, to January 31, 1932, it expended for capital purposes upon its properties and the properties of its subsidiaries the sum of $16,596,058.10 not theretofore used as a basis for capitalization.

The applicant states that if to this amount there be added the $10,183,641.90 above mentioned as having been expended in constructing the Northern California extension, the expenditures submitted in this and the previous applications would total $26,779,700. It is asserted that should there be deducted from that amount $1,303,679.79 which might not be considered properly capitalizable, consisting of sinking funds $326.02, deposits in lieu of mortgaged property sold $710.50, subscription to capital stock of Western Pacific California Railroad Company $27,500, Railway Express Agency capital stock $200, advances to subsidiary companies for other than capital purposes

$919,076.37, other advances $270,977.57, and other investments $84,889.33, there would remain $25,476,020.21 of expenditures, against which there has been issued and outstanding $19,999,500 of bonds, leaving $5,476,520.21 to support the proposed issue of $5,000,000 of series-B bonds.

To finance the cost of constructing its Northern California extension, the applicant was authorized to issue $19,000,000 of securities, consisting of $5,000,000 of first-mortgage gold bonds in *Western Pac. R. Co. Bonds, supra,* and $5,000,000 of 5 per cent gold debentures in *Western Pac. R. Co. Debentures,* 166 I. C. C. 720. As was indicated in *Western Pac. R. Co. Securities, supra,* and supplemental report therein, 184 I. C. C. 13, the applicant was authorized to issue to retire the 5 per cent debentures a promissory note or notes for not exceeding $5,000,000, to be secured by the pledge of not exceeding $6,250,000 of general and refunding mortgage gold bonds, series A. The applicant shows that the debentures have been retired by the issue of $4,999,800 of 3-year notes and a cash payment of $200. In the original report in the proceeding last cited, we stated that the issue of notes to retire the debentures was in the nature of temporary financing and that $5,000,000 of the series-A bonds therein authorized should be regarded as being issued to retire the debentures. Accordingly there has been authorized against the total expenditures above mentioned $5,000,000 of first-mortgage gold bonds and $15,000,000 of general and refunding mortgage gold bonds, series A, although the applicant has issued only $14,999,500 of the series-A bonds. Deducting from $25,476,020.21 the $20,000,000 of bonds authorized would leave $5,476,020.21 of expenditures as support for the series-B bonds. However, our examination of the expenditures made during the period July 14, 1916, to January 31, 1932, amounting to $16,596,058.10, discloses many duplications of expenditures submitted in prior applications as support for the issue of securities therein

sought, so that until these seeming discrepancies have been accounted for by the applicant, which has been requested of it, we are unable to accept as a basis for the issue of additional bonds the $5,476,020.21 of expenditures mentioned above.

Therefore, for the purposes of this application it will be necessary for us to consider as a basis for the issue of the series-B bonds the excess of capital assets over capital liabilities as shown by the applicant's general balance sheet as of May 31, 1932, and certain analytical statements. These assets and liabilities are as follows: Investment in road and equipment $139,226,500.53 less accrued depreciation, equipment, $7,885,379.55, net investment in road and equipment $131,341,120.98, miscellaneous physical property $1,029,513.85, investment in affiliated companies pledged under applicant's first mortgage $8,625,454, investment in affiliated companies pledged under applicant's general and refunding mortgage $2,642,648.38, advances to affiliated companies for additions and betterments (including $27,500 subscription to capital stock of the Western Pacific California Railroad Company), $2,276,316.04, working capital $2,880,994.35, consisting of cash $737,322.30 and material and supplies $2,143,672.05, total capital assets $148,796,047.60, common stock $47,500,000, preferred stock $28,300,000, first-mortgage 5 per cent gold bonds $49,290,100, general and refunding mortgage gold bonds, series A, $14,999,500, equipment-trust certificates $4,550,000, total capital liabilities $144,639,600.

The balance sheet shows investment in miscellaneous physical property in the amount of $1,817,379.03. The amount shown above as capitalizable consists of $862,429.18 representing property at Oakland, Calif., acquired for the purpose of relocating the applicant's main line and $167,084.67 representing leased track material. The remainder of the balance sheet figure for miscellaneous physical property represents investments in property of a character

not considered as affording a proper basis for capitalization. In addition to the amounts given above for advances to affiliated companies, the general balance sheet figures include, under investment in affiliated companies unpledged, other advances not considered as capitalizable and several small items representing investment in the capital stock of various companies. The sum of these items is $1,832,460.63, and consists principally of $1,383,477.43 of advances to carrier companies for purposes other than for additions and betterments, and $413,598.53 of advances to a land company. The general balance sheet shows none of the general and refunding mortgage bonds to be outstanding, but does show outstanding $4,999,800 of notes payable to A. C. James Company, and $2,102,000 of notes payable to the Reconstruction Finance Corporation. These notes are secured by the pledge of general and refunding mortgage bonds, series A, issued against capital expenditures. Therefore, for the purpose of comparing capital assets and liabilities, the primary obligations consisting of the notes have been excluded and instead there have been included the general and refunding mortgage bonds constituting the collateral security therefor.

The excess of capital assets over capital liabilities, as shown above, is $4,156,447.60, which may be accepted as a proper basis for additional capitalization and in respect of which the applicant may issue not exceeding $4,000,000 of the proposed bonds. Ordinarily, advances to affiliated companies carried in open account would not constitute an appropriate basis for the issue of capital securities, but inasmuch as the applicant included in the expenditures to January 31, 1932, amounting to $16,596,058.10, the expenditures made for additions and betterments to the properties of its affiliated companies, the advances from which such expenditures were made may, in this instance, be considered as capital assets upon condition that the applicant require the affiliated companies, upon due authorization,

to issue to it their capital stock, bonds, notes, or other obligations in payment and settlement of the advances, such securities upon their delivery to the applicant forthwith to be pledged with the trustee of its general and refunding mortgage dated January 1, 1932. The order to be entered herein will require that this be done.

As indicated above, the applicant requests authority to pledge the bonds as collateral security for two notes payable to the Finance Corporation and for the payment of any other liability or liabilities due or to become due, or which may hereafter be contracted or existing. As under the provisions of section 5 of the Reconstruction Finance Corporation Act, no authorization under section 20a of the interstate commerce act is necessary for the applicant to pledge its bonds as collateral for notes issued to evidence loans from the Finance Corporation, that part of the application will be dismissed.

The applicant also seeks authority to pledge its equity in the proposed bonds, subject to their pledge to the Finance Corporation, to the Credit Corporation for a note for $1,303,000 payable to that corporation, or order, on demand, but, if no demand is made, then on or before February 28, 1934, and any extension or renewal thereof, and for various other existing or possible obligations to the Credit Corporation. Our authorization herein will be limited to the pledge of the applicant's equity in the proposed bonds as security for the $1,303,000 note or any extension or renewal thereof.

We find that, subject to the condition indicated above, the proposed issue by The Western Pacific Railroad Company of not exceeding $4,000,000 of general and refunding mortgage gold bonds, series B, and the pledge by it of its equity therein, as collateral security for a note of $1,303,000 or any extension or renewal thereof, to the Railroad Credit Corporation as aforesaid (*a*) are for lawful objects within

its corporate purposes, and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (*b*) are reasonably necessary and appropriate for such purposes.

An appropriate order will be entered.

THE WESTERN PACIFIC RAILROAD COMPANY
SACRAMENTO NORTHERN RAILWAY
TIDEWATER SOUTHERN RAILWAY COMPANY
DEEP CREEK RAILROAD COMPANY (c)

OPERATING RESULTS-COMBINED
(All Inter-Company Items Eliminated)

ITEM OR ACCOUNT	MONTH OF DECEMBER		Increase or Decrease.		PERIOD JANUARY 1 TO DEC	
	1940	1939	Amount	Per Cent	1940	1939
AVERAGE MILEAGE OR ROAD OPERATED	1,536.19	1,545.09	8.90	.58	1,547.00	1,571.92
OPERATING REVENUES						
Freight	$ 1,718,568.29	$ 1,351,283.31	$ 367,284.98	27.18	$ 18,701,678.52	$ 16,819,156.81
Passenger	73,747.22	56,303.33	17,443.89	30.98	860,046.90	1,014,887.10
Mail	4,893.72	6,115.30	1,221.58	19.98	41,830.53	45,135.06
Express	8,069.86	5,693.10	2,376.76	64.36	79,282.94	92,722.02
Dining Car, Hotel & Restaurant	8,049.54	5,076.44	2,973.10	58.57	82,231.30	97,561.41
Miscellaneous	19,025.36	18,236.36	786.91	4.31	233,271.80	238,059.06
Total Railway Operating Revenues	$ 1,830,363.89	$ 1,440,709.83	$ 389,644.06	27.05	$ 19,998,341.99	$ 18,307,521.45
OPERATING EXPENSES						
Maintenance of Way & Structures	$ 171,912.36	$ 209,115.24	$ 37,202.88	17.79	$ 3,082,805.73	$ 2,809,949.28
Maintenance of Equipment	246,236.01	262,768.04	16,533.03	6.29	2,820,508.72	3,097,290.12
Power	7,860.59	10,994.80	3,134.21	28.51	129,216.59	146,921.44
Traffic	64,792.76	64,192.52	600.24	.94	788,256.19	795,026.73
Transportation - Rail Line	684,360.24	610,015.57	74,534.67	12.22	7,367,110.31	7,033,671.20
Miscellaneous Operations	10,985.96	8,934.10	2,051.86	22.97	127,300.68	146,974.66
General	64,039.87	59,379.19	4,660.68	7.85	935,849.22	768,142.50
Transportation for Investment - Credit	3,769.77	3,312.59	457.18	13.80	11,653.55	9,529.91
Total Railway Operating Expenses	$ 1,246,607.02	$ 1,222,086.87	$ 24,520.15	2.01	$ 15,239,393.89	$ 14,778,446.02
NET REVENUE FROM RAILWAY OPERATIONS	$ 583,746.87	$ 218,622.96	$ 365,123.91	167.01	$ 4,758,948.10	$ 3,529,075.43
Excise and Use Tax Accruals	$ 41,933.18	$ 38,077.09	$ 3,856.09	10.13	$ 534,791.71	$ 498,429.69
Railway Tax Accruals - All Other	52,190.72	47,365.16	4,825.56	10.19	636,028.15	633,816.62
Railway Operating Income	$ 489,622.97	$ 133,180.71	$ 356,442.26	267.64	$ 3,588,128.24	$ 2,396,829.12
Hire of Equipment - Net Debit	$ 137,066.76	$ 116,035.63	$ 21,031.13	18.12	$ 1,338,079.09	$ 1,179,970.54
Joint Facility Rents - Net Credit	19,404.61	12,778.18	6,626.43	51.86	139,141.08	126,926.42
Net Railway Operating Income	$ 371,960.82	$ 29,923.26	$ 342,037.56	-	$ 2,389,190.23	$ 1,343,785.00
NON-OPERATING INCOME						
Rental of Property	$ 22,151.30	$ 23,967.33	$ 1,816.03	7.58	$ 296,247.83	$ 245,113.20
Interest Accruals	2,983.77	2,313.91	669.86	28.95	30,167.44	23,825.23
Miscellaneous	14,235.63	2,954.42	14,190.05	-	2,569.34	4,669.80
Total Non-Operating Income	$ 13,899.44	$ 29,235.66	$ 15,336.22	52.46	$ 327,984.61	$ 313,608.23
GROSS INCOME	$ 385,860.26	$ 59,158.92	$ 326,701.34	552.24	$ 2,717,174.84	$ 1,657,393.23
MISCELLANEOUS DEDUCTIONS						
Miscellaneous Rents	$ 2,579.16	$ 2,579.16	$ -	-	$ 31,038.93	$ 30,895.46
Miscellaneous Tax Accruals	5,459.03	5,180.98	278.05	5.37	59,655.47	59,564.55
Amortization of Discount	11,352.25	12,251.27	899.02	7.34	136,706.42	137,903.98
Miscellaneous	4,965.47	9,460.61	4,495.14	47.51	23,316.52	44,514.71
Total Miscellaneous Deductions	$ 24,355.91	$ 29,472.02	$ 5,116.11	17.36	$ 204,084.30	$ 272,878.70
AVAILABLE FOR INTEREST	$ 361,504.35	$ 29,686.90	$ 331,817.45	-	$ 2,513,090.54	$ 1,384,514.53
Interest on Funded Debt	$ 304,373.62	$ 238,930.65	$ 65,442.97	27.39	$ 3,653,106.90	$ 2,870,913.26
					47,976.94	839,515.62

THE WESTERN PACIFIC RAILROAD COMPANY
SACRAMENTO NORTHERN RAILWAY
TIDEWATER SOUTHERN RAILWAY COMPANY
DEEP CREEK RAILROAD COMPANY (*)

OPERATING RESULTS-COMBINED
(All Inter-Company Items Eliminated)

ITEM OR ACCOUNT	MONTH OF DECEMBER				PERIOD JANUARY 1 TO DECEMBER 31			
			Increase or *Decrease.*				Increase or *Decrease.*	
	1940	1939	Amount	Per Cent	1940	1939	Amount	Per Cent
AVERAGE MILEAGE OR ROAD OPERATED	1,536.19	1,545.09	*8.90*	*.58*	1,547.00	1,571.92	*24.92*	*1.59*
OPERATING REVENUES								
Freight	$ 1,718,568.29	$ 1,351,283.31	$ 367,284.98	27.18	$ 18,701,678.52	$ 16,819,156.81	$ 1,882,521.71	11.19
Passenger	73,747.22	56,303.33	17,443.89	30.98	860,046.90	1,014,887.10	*154,840.20*	*15.26*
Mail	4,893.72	6,115.30	*1,221.58*	*19.98*	41,830.53	45,135.05	*3,304.52*	*7.32*
Express	6,069.86	3,693.10	2,376.76	64.36	79,282.94	92,722.02	*13,439.08*	*14.49*
Dining Car, Hotel & Restaurant	8,049.54	5,076.44	2,973.10	58.57	82,231.30	97,561.41	*15,330.11*	*15.71*
Miscellaneous	19,025.26	18,238.35	786.91	4.31	233,271.80	238,059.06	*4,787.26*	*2.01*
Total Railway Operating Revenues	$ 1,830,353.89	$ 1,440,709.83	$ 389,644.06	27.05	$ 19,998,341.99	$ 18,307,521.45	$ 1,690,820.54	9.24
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 171,912.36	$ 209,115.24	*$ 37,202.88*	*17.79*	$ 3,082,805.73	$ 2,809,949.28	$ 272,856.45	9.71
Maintenance of Equipment	246,235.01	262,768.04	*16,533.03*	*6.29*	2,820,508.72	3,097,290.12	*276,781.40*	*8.94*
Power	7,860.59	10,994.80	*3,134.21*	*28.51*	129,216.59	146,921.44	*17,704.85*	*12.05*
Traffic	64,792.76	64,192.52	600.24	.94	788,256.19	735,026.73	3,229.46	.41
Transportation - Rail Line	684,550.24	610,015.57	74,534.67	12.22	7,367,110.31	7,033,671.20	333,439.11	4.74
Miscellaneous Operations	10,985.96	8,934.10	2,051.86	22.97	127,300.68	146,974.66	*19,673.98*	*13.39*
General	64,039.87	59,379.19	4,660.68	7.85	935,849.22	768,142.50	167,706.72	21.83
Transportation for Investment - Credit	3,769.77	3,312.59	457.18	13.80	11,653.55	9,529.91	2,123.64	22.28
Total Railway Operating Expenses	$ 1,246,607.02	$ 1,222,086.87	$ 24,520.15	2.01	$ 15,239,393.89	$ 14,778,446.02	$ 460,947.87	3.12
NET REVENUE FROM RAILWAY OPERATIONS	$ 583,746.87	$ 218,622.96	$ 365,123.91	167.01	$ 4,758,948.10	$ 3,529,075.43	$ 1,229,872.67	34.85
Excise and Use Tax Accruals	$ 41,933.18	$ 38,077.09	$ 3,856.09	10.13	$ 534,791.71	$ 498,429.69	$ 36,362.02	7.30
Railway Tax Accruals - All Other	52,190.72	47,365.16	4,825.56	10.19	636,028.15	633,816.62	2,211.53	.35
Railway Operating Income	$ 489,622.97	$ 133,180.71	$ 356,442.26	267.64	$ 3,588,128.24	$ 2,396,829.12	$ 1,191,299.12	49.70
Hire of Equipment - Net Debit	$ 137,066.76	$ 116,038.63	$ 21,031.13	18.12	$ 1,338,079.09	$ 1,179,970.54	$ 158,108.55	13.40
Joint Facility Rents - Net Credit	19,404.61	12,778.18	6,626.43	51.86	139,141.08	126,926.42	12,214.66	9.62
Net Railway Operating Income	$ 371,960.82	$ 29,923.26	$ 342,037.56	-	$ 2,389,190.23	$ 1,343,785.00	$ 1,045,405.23	77.80
NON-OPERATING INCOME								
Rental of Property	$ 22,151.30	$ 23,967.33	*$ 1,816.03*	*7.58*	$ 295,947.83	$ 245,113.20	$ 10,134.63	3.56
Interest Accruals	2,983.77	2,313.91	669.86	28.95	30,167.44	23,825.23	6,342.21	26.62
Miscellaneous	*11,235.63*	2,954.42	*14,190.05*	-	2,569.34	4,669.80	*2,100.46*	*44.98*
Total Non-Operating Income	$ 13,899.44	$ 29,235.66	*$ 15,336.22*	*52.46*	$ 327,984.61	$ 313,608.23	$ 14,376.38	4.58
GROSS INCOME	$ 385,860.26	$ 59,158.92	$ 326,701.34	552.24	$ 2,717,174.84	$ 1,657,393.23	$ 1,059,781.61	63.94
MISCELLANEOUS DEDUCTIONS								
Miscellaneous Rents	$ 2,579.16	$ 2,579.16	$ -	-	$ 31,038.93	$ 30,895.46	$ 143.47	.46
Miscellaneous Tax Accruals	5,459.03	5,180.98	278.05	5.37	59,655.47	59,564.55	90.92	.15
Amortization of Discount	11,352.26	12,251.27	*899.02*	*7.34*	136,706.42	137,903.98	*1,197.56*	*.87*
Miscellaneous	4,965.47	9,460.61	*4,495.14*	*47.51*	*23,316.52*	44,514.71	*67,831.23*	-
Total Miscellaneous Deductions	$ 24,355.91	$ 29,472.02	*$ 5,116.11*	*17.36*	$ 204,084.30	$ 272,878.70	*$ 68,794.40*	*25.21*
AVAILABLE FOR INTEREST	$ 361,504.35	$ 29,686.90	$ 331,817.45	-	$ 2,513,090.54	$ 1,384,514.53		
Interest on Funded Debt	$ 304,373.62	$ 238,930.65	$ 65,442.97	27.39	$ 3,653,108.90	$ 2,870,913.26		
Interest on Unfunded Debt	6,081.51	71,098.82	*65,017.31*	*91.45*	47,976.94	839,515.62		
Total Interest Deductions	$ 310,455.13	$ 310,029.47	$ 425.66	.14	$ 3,701,083.84	$ 3,710,428.88		
NET INCOME	$ 51,049.22	*$ 280,342.57*	$ 331,391.79	-	*$ 1,187,993.30*	*$ 2,325,914.35*		

NOTE: Italics denote red.

(*) - Deep Creek Railroad Company discontinued operations effective July 31, 1939

Accounting Department
San Francisco, California
February 3, 1941

1940	1939	Amount	Per Cent	1940	1939	Amount	Per Cent
1,536.19	1,545.09	8.90	.58	1,547.00	1,571.92	24.92	1.59
2,718,568.29	$ 1,351,283.31	$ 367,284.98	27.18	$ 18,701,678.52	$ 16,819,156.81	$ 1,882,521.71	11.19
73,747.22	56,303.33	17,443.89	30.98	860,046.90	1,014,887.10	154,840.20	15.26
4,893.72	6,115.30	1,221.58	19.98	41,830.53	45,135.05	3,304.52	7.32
6,069.86	3,693.10	2,376.76	64.36	79,282.94	92,722.02	13,439.08	14.49
8,049.54	5,076.44	2,973.10	58.57	82,231.30	97,561.41	15,330.11	15.71
19,025.96	18,238.35	786.91	4.31	233,271.80	238,059.06	4,787.26	2.01
1,830,363.89	$ 1,440,709.83	$ 389,644.06	27.05	$ 19,998,341.99	$ 18,307,521.45	$ 1,690,820.54	9.24
171,912.36	$ 209,115.24	$ 37,202.88	17.79	$ 3,082,805.73	$ 2,809,949.28	$ 272,856.45	9.71
246,236.01	262,768.04	16,533.03	6.29	2,820,508.72	3,097,290.12	276,781.40	8.94
7,860.59	10,994.80	3,134.21	28.51	129,216.69	146,921.44	17,704.85	12.05
64,792.76	64,192.52	600.24	.94	788,256.19	785,026.73	3,229.46	.41
684,550.24	610,015.57	74,534.67	12.22	7,367,110.31	7,033,671.20	333,439.11	4.74
10,985.96	8,934.10	2,051.86	22.97	127,300.68	146,974.66	19,673.98	13.39
64,039.87	59,379.19	4,660.68	7.85	935,849.22	768,142.50	167,706.72	21.83
3,769.77	3,312.59	457.18	13.80	11,653.55	9,529.91	2,123.64	22.28
1,246,607.02	$ 1,222,086.87	$ 24,520.15	2.01	$ 15,239,393.89	$ 14,778,446.02	$ 460,947.87	3.12
583,746.87	$ 218,622.96	$ 365,123.91	167.01	$ 4,758,948.10	$ 3,529,075.43	$ 1,229,872.67	34.85
41,933.18	$ 38,077.09	$ 3,856.09	10.13	$ 534,791.71	$ 498,429.69	$ 36,362.02	7.30
52,190.72	47,365.16	4,825.56	10.19	636,028.15	633,816.62	2,211.53	.35
489,622.97	$ 133,180.71	$ 356,442.26	267.64	$ 3,588,128.24	$ 2,396,829.12	$ 1,191,299.12	49.70
137,066.76	$ 116,035.63	$ 21,031.13	18.12	$ 1,338,079.09	$ 1,179,970.54	$ 158,108.55	13.40
19,404.61	12,778.18	6,626.43	51.86	139,141.08	126,926.42	12,214.66	9.62
371,960.82	$ 29,923.26	$ 342,037.56	-	$ 2,389,190.23	$ 1,343,785.00	$ 1,045,405.23	77.80
22,151.30	$ 23,967.33	$ 1,816.03	7.58	$ 295,247.83	$ 285,113.20	$ 10,134.63	3.55
2,983.77	2,313.91	669.86	28.95	30,167.44	23,825.23	6,342.21	26.62
11,235.63	2,954.42	14,190.05	-	2,569.34	4,669.80	2,100.46	44.98
13,899.44	$ 29,235.66	$ 15,336.22	52.46	$ 327,984.61	$ 313,608.23	$ 14,376.38	4.58
385,860.26	$ 59,158.92	$ 326,701.34	552.24	$ 2,717,174.84	$ 1,657,393.23	$ 1,059,781.61	63.94
2,579.16	$ 2,579.16	$ -	-	$ 31,638.93	$ 30,895.46	$ 743.47	.46
5,459.03	5,180.98	278.05	5.37	89,655.47	89,564.55	90.92	.85
11,352.25	12,251.27	899.02	7.34	136,706.42	137,903.98	1,197.56	.87
4,965.47	9,460.61	4,495.14	47.51	23,316.52	44,514.71	67,831.23	-
24,355.91	$ 29,472.02	$ 5,116.11	17.36	$ 204,084.30	$ 272,878.70	$ 68,794.40	25.21
361,504.35	$ 29,686.90	$ 331,817.45	-	$ 2,513,090.54	$ 1,384,514.53	$ 1,128,576.01	81.51
304,373.62	$ 238,930.65	$ 65,442.97	27.39	$ 3,653,106.90	$ 2,870,913.26	$ 782,193.64	27.25
6,081.51	71,098.82	65,017.31	91.45	47,976.94	839,515.62	791,538.68	94.29
310,455.13	$ 310,029.47	$ 425.66	.14	$ 3,701,083.84	$ 3,710,428.88	$ 9,345.04	.25
51,049.22	$ 280,342.57	$ 331,391.79	-	$ 1,187,993.30	$ 2,325,914.35	$ 1,137,921.05	-

31, 1939

THE WESTERN PACIFIC RAILROAD COMPANY

SACRAMENTO NORTHERN RAILWAY

TIDEWATER SOUTHERN RAILWAY COMPANY

OPERATING RESULTS-COMBINED

(All Inter-Company Items Eliminated)

ITEM OR ACCOUNT	MONTH OF DECEMBER				PERIOD JANUARY 1 to DECEMBER 31			
	1941	1940	Increase or *Decrease.* Amount	Per Cent	1941	1940	Increase or *Decrease.* Amount	Per Cent
AVERAGE MILEAGE OF ROAD OPERATED	1,536.19	1,536.19	-	-	1,536.19	1,547.00	*10.81*	*.70*
OPERATING REVENUES								
Freight	$ 2,279,243.48	$ 1,718,568.29	$ 560,675.19	32.62	$ 24,119,568.04	$ 18,701,678.52	$ 5,417,889.52	28.97
Passenger	122,803.41	73,747.22	49,056.19	66.52	873,173.63	860,046.90	13,126.73	1.53
Mail	3,886.06	4,893.72	*1,007.66*	*20.59*	36,898.35	41,830.53	*4,932.18*	*11.79*
Express	5,367.08	6,069.86	*702.78*	*11.58*	70,325.59	79,282.94	*8,957.35*	*11.30*
Dining Car, Hotel & Restaurant	13,930.64	8,049.54	5,881.10	73.06	125,898.78	82,231.30	43,667.48	53.10
Miscellaneous	35,686.07	19,025.26	16,660.81	87.57	320,618.24	233,271.80	87,346.44	37.44
Total Railway Operating Revenues	$ 2,460,916.74	$ 1,830,353.89	$ 630,562.85	34.45	$ 25,546,482.63	$ 19,998,341.99	$ 5,548,140.64	27.74
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 411,392.64	$ 171,912.36	$ 239,480.28	139.30	$ 3,115,547.19	$ 3,082,805.73	$ 32,741.46	1.06
Maintenance of Equipment	403,667.40	246,235.01	157,432.39	63.94	3,873,731.31	2,820,508.72	1,053,222.59	37.34
Power	7,293.22	7,860.59	*567.37*	*7.22*	88,380.60	129,216.59	*40,835.99*	*31.60*
Traffic	86,625.77	64,792.76	21,833.01	33.70	872,011.66	788,256.19	83,755.47	10.63
Transportation - Rail Line	1,140,972.01	684,550.24	456,421.77	66.67	9,159,206.62	7,367,110.31	1,792,096.31	24.33
Miscellaneous Operations	20,669.69	10,985.96	9,683.73	88.15	167,073.93	127,300.68	39,773.25	31.24
General	91,895.77	64,039.87	27,855.90	43.50	794,896.43	935,849.22	*140,952.79*	*15.06*
Transportation for Investment - Credit	1,545.36	3,769.77	*2,224.41*	*59.00*	10,214.70	11,653.55	*1,438.85*	*12.35*
Total Railway Operating Expenses	$ 2,160,971.14	$ 1,246,607.02	$ 914,364.12	73.36	$ 18,060,633.04	$ 15,239,393.89	$ 2,821,239.15	18.51
NET REVENUE FROM RAILWAY OPERATIONS	$ 299,945.60	$ 583,746.87	$ *283,801.27*	*48.62*	$ 7,485,849.59	$ 4,758,948.10	$ 2,726,901.49	57.30
Excise and Use Tax Accruals	$ 86,343.42	$ 41,933.18	$ 44,410.24	105.91	$ 644,779.33	$ 534,791.71	$ 109,987.62	20.57
Railway Tax Accruals - All Other	157,667.16	52,190.72	105,476.44	202.10	1,072,774.23	636,028.15	436,746.08	68.67
Railway Operating Income	$ 55,935.02	$ 489,622.97	$ *433,687.95*	*88.58*	$ 5,768,296.03	$ 3,588,128.24	$ 2,180,167.79	60.76
Hire of Equipment - Net Debit	$ 179,298.88	$ 137,066.76	$ 42,231.92	30.81	$ 1,711,134.09	$ 1,338,079.09	$ 373,055.00	27.88
Joint Facility Rents - Net Credit	17,104.56	19,404.61	*2,300.05*	*11.85*	145,757.64	139,141.08	6,616.56	4.76
Net Railway Operating Income	$ *106,259.10*	$ 371,960.82	$ *478,219.92*	*128.57*	$ 4,202,919.58	$ 2,389,190.23	$ 1,813,729.35	75.91
NON-OPERATING INCOME								
Rental of Property	$ 45,682.59	$ 22,151.30	$ 23,531.29	106.23	$ 398,533.56	$ 295,247.83	$ 103,285.73	34.98
Interest Accruals	2,589.89	5,983.77	*393.88*	*13.20*	41,813.41	30,167.44	11,645.97	38.60
Miscellaneous	37,250.02	*11,235.69*	48,485.66	-	39,945.81	2,569.34	37,376.47	-
Total Non-Operating Income	$ 85,522.50	$ 13,899.44	$ 71,623.06	515.30	$ 480,292.78	$ 327,984.61	$ 152,308.17	46.44
GROSS INCOME	$ *20,736.60*	$ 385,860.26	$ *406,596.86*	*105.37*	$ 4,683,212.36	$ 2,717,174.84	$ 1,966,037.52	72.36
MISCELLANEOUS DEDUCTIONS								
Miscellaneous Rents	$ 2,321.78	$ 2,279.16	$ 42.62	1.87	$ 27,261.84	$ 27,438.93	$ *177.09*	*.65*
Miscellaneous Tax Accruals	5,738.91	5,459.03	279.88	5.13	61,840.02	59,655.47	2,184.55	3.66
Miscellaneous	18,756.60	4,965.47	13,791.13	277.74	42,372.57	*23,316.52*	65,689.09	-
Total Miscellaneous Deductions	$ 26,817.29	$ 12,703.66	$ 14,113.63	111.10	$ 131,474.43	$ 63,777.88	$ 67,696.55	106.14
AVAILABLE FOR FIXED CHARGES	$ *47,553.89*	$ 373,156.60	$ *420,710.49*	*112.74*	$ 4,551,737.93	$ 2,653,396.96	$ 1,898,340.97	71.54
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	$ -	-	$ 3,600.00	$ 3,600.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	$ 205,375.41	$ 205,375.41	$ -	-	$ 2,464,505.00	$ 2,464,505.00	$ -	-
Equipment Obligations do	5,352.56	5,542.60	*190.04*	*3.43*	62,223.39	70,029.18	*7,805.79*	*11.15*
Trustees' Certificates do	16,122.22	33,311.11	*17,188.89*	*51.60*	379,794.43	399,977.78	*20,183.35*	*5.05*
Other Obligations (*)	62,255.49	60,144.50	2,110.99	3.51	743,529.71	718,594.94	24,934.77	3.47
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	364.99	688.50	*323.51*	*46.99*	5,515.31	9,613.27	*4,097.96*	*42.63*
Other Obligations	2,418.69	5,393.01	*2,974.32*	*55.15*	6,015.10	38,363.67	*32,348.57*	*84.32*
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.49	11,283.49	-	-	135,401.88	136,401.88	*1,000.00*	*.73*
Equipment Obligations do	109.06	68.76	40.30	58.61	975.97	304.54	671.43	220.50
Total Fixed Charges	$ 303,581.91	$ 322,107.38	$ *18,525.47*	*5.75*	$ 3,801,560.79	$ 3,841,390.26	$ *39,829.47*	*1.04*
NET INCOME	$ *351,135.80*	$ 51,049.22	$ *402,185.02*	*787.84*	$ 750,177.14	$ *1,187,993.30*	$ 1,938,170.44	-

AVERAGE MILEAGE OF ROAD OPERATED	1,536.19	1,536.19		-	1,536.19	1,547.00	10.81	.70
OPERATING REVENUES								
Freight	$ 2,279,243.48	$ 1,718,568.29	$ 560,675.19	32.62	$ 24,119,566.04	$ 18,701,678.52	$ 5,417,889.52	28.97
Passenger	122,803.41	73,747.22	49,056.19	66.52	873,173.63	860,046.90	13,126.73	1.53
Mail	3,886.06	4,893.72	*1,007.66*	*20.59*	36,898.36	41,830.53	*4,932.18*	*11.79*
Express	5,367.08	6,069.86	*702.78*	*11.58*	70,395.89	79,283.94	*8,957.35*	*11.30*
Dining Car, Hotel & Restaurant	13,930.64	8,049.54	5,881.10	73.06	125,898.78	82,231.30	43,667.48	53.10
Miscellaneous	35,686.07	19,025.26	16,660.81	87.57	320,618.24	233,271.80	87,346.44	37.44
Total Railway Operating Revenues	$ 2,460,916.74	$ 1,830,353.89	$ 630,562.85	34.45	$ 25,546,482.63	$ 19,998,341.99	$ 5,548,140.64	27.74
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 411,392.64	$ 171,912.36	$ 239,480.28	139.30	$ 3,115,547.19	$ 3,082,805.73	$ 32,741.46	1.06
Maintenance of Equipment	403,667.40	246,236.01	157,432.39	63.94	3,873,731.31	2,820,508.72	1,053,222.59	37.34
Power	7,293.22	7,860.59	*567.37*	*7.22*	88,360.60	129,216.59	*40,855.99*	*31.60*
Traffic	86,625.77	64,792.76	21,833.01	33.70	872,011.66	788,256.19	83,755.47	10.63
Transportation - Rail Line	1,140,972.01	684,550.24	456,421.77	66.67	9,159,206.82	7,367,110.31	1,792,096.51	24.33
Miscellaneous Operations	20,669.69	10,985.96	9,683.73	88.15	167,073.93	127,300.68	39,773.25	31.24
General	91,895.77	64,039.87	27,855.90	43.50	794,896.43	935,849.22	*140,952.79*	*15.06*
Transportation for Investment - Credit	1,545.36	3,769.77	*2,224.41*	*59.00*	10,214.70	11,653.55	*1,438.85*	*12.35*
Total Railway Operating Expenses	$ 2,160,971.14	$ 1,246,607.02	$ 914,364.12	73.35	$ 18,060,633.04	$ 15,239,393.89	$ 2,821,239.15	18.51
NET REVENUE FROM RAILWAY OPERATIONS	$ 299,945.60	$ 583,746.87	$ *283,801.27*	*48.62*	$ 7,485,849.59	$ 4,758,948.10	$ 2,726,901.49	57.30
Excise and Use Tax Accruals	$ 86,343.42	$ 41,933.18	$ 44,410.24	105.91	$ 644,779.33	$ 534,791.71	$ 109,987.62	20.57
Railway Tax Accruals - All Other	157,667.16	52,190.72	105,476.44	202.10	1,072,774.23	636,028.15	436,746.08	68.67
Railway Operating Income	$ 55,935.02	$ 489,622.97	$ *433,687.95*	*88.58*	$ 5,768,296.03	$ 3,588,128.24	$ 2,180,167.79	60.76
Hire of Equipment - Net Debit	$ 179,298.68	$ 137,066.76	$ 42,231.92	30.81	$ 1,711,134.09	$ 1,338,079.09	$ 373,055.00	27.88
Joint Facility Rents - Net Credit	17,104.56	19,404.61	*2,300.05*	*11.85*	145,757.64	139,141.08	6,616.56	4.76
Net Railway Operating Income	$ *106,259.10*	$ 371,960.82	$ *478,219.92*	*128.57*	$ 4,202,919.58	$ 2,389,190.23	$ 1,813,729.35	75.91
NON-OPERATING INCOME								
Rental of Property	$ 45,682.59	$ 22,151.30	$ 23,531.29	106.23	$ 348,533.56	$ 295,247.83	$ 103,285.73	34.98
Interest Accruals	2,589.89	2,983.77	*393.88*	*13.20*	41,813.41	30,167.44	11,645.97	38.60
Miscellaneous	37,250.02	*11,235.63*	48,485.65	-	39,945.81	2,569.34	37,376.47	-
Total Non-Operating Income	$ 85,522.50	$ 13,899.44	$ 71,823.06	516.30	$ 480,292.78	$ 327,984.61	$ 152,308.17	46.44
GROSS INCOME	$ *20,736.60*	$ 385,860.25	$ *406,596.86*	*105.37*	$ 4,683,212.36	$ 2,717,174.84	$ 1,966,037.52	72.36
MISCELLANEOUS DEDUCTIONS								
Miscellaneous Rents	$ 2,321.78	$ 2,279.16	$ 42.62	1.87	$ 27,261.84	$ 27,438.93	$ *177.09*	.65
Miscellaneous Tax Accruals	5,738.91	5,459.03	279.88	5.13	61,840.02	59,655.47	2,184.55	3.66
Miscellaneous	18,756.60	4,965.47	13,791.13	277.74	42,372.57	*23,316.52*	66,689.09	-
Total Miscellaneous Deductions	$ 26,817.29	$ 12,703.66	$ 14,113.63	111.10	$ 131,474.43	$ 63,777.88	$ 67,696.55	106.14
AVAILABLE FOR FIXED CHARGES	$ *47,553.89*	$ 373,156.60	$ *420,710.49*	*112.74*	$ 4,551,737.93	$ 2,653,396.96	$ 1,898,340.97	71.54
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	$ -	-	$ 3,600.00	$ 3,600.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	$ 205,375.41	$ 205,375.41	$ -	-	$ 2,464,505.00	$ 2,464,505.00	$ -	-
Equipment Obligations do	5,359.56	5,542.60	*190.04*	*3.43*	62,283.39	70,029.18	*7,805.79*	*11.15*
Trustees' Certificates d	16,122.22	33,311.11	*17,188.89*	*51.60*	379,794.43	399,977.78	*20,183.35*	*5.05*
Other Obligations (*)	62,255.49	60,144.50	2,110.99	3.51	743,529.71	718,594.94	24,934.77	3.47
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	384.99	688.50	*323.51*	*46.99*	5,515.31	9,613.27	*4,097.96*	*42.63*
Other Obligations	2,418.69	5,393.01	*2,974.32*	*55.15*	6,015.10	38,363.67	*32,348.57*	*84.32*
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.49	11,283.49	-	-	135,401.88	136,401.88	*1,000.00*	.73
Equipment Obligations do	109.06	68.76	40.30	58.61	975.97	304.54	671.43	220.50
Total Fixed Charges	$ 303,581.91	$ 322,107.38	$ *18,525.47*	*5.75*	$ 3,801,560.79	$ 3,841,390.26	$ *39,829.47*	*1.04*
NET INCOME	$ *351,135.80*	$ 51,049.22	$ *402,185.02*	*787.84*	$ 750,177.14	$ *1,187,993.30*	$ 1,938,170.44	-

NOTE: - Italics denote loss.

Accounting Department
San Francisco, California
February 7th, 1942

Note (*) - "Interest on Funded Debt - Other Obligations" includes the following:

		Month		Period	
		1941	1940	1941	1940
Notes Payable	- Reconstruction Finance Corporation	$12,582.61	$12,582.61	$148,149.97	$148,555.84
" "	- A. C. James Co.	20,832.50	20,832.50	249,990.00	249,990.00
" "	- Railroad Credit Corporation	2,105.93	-	24,795.74	-
Advances	- The Western Pacific Railroad Corporation	22,894.80	22,894.80	274,736.10	274,736.10
"	- The Western Realty Company	208.35	208.35	2,500.00	2,500.00
"	- The Western Pacific Railroad Corporation to Sacramento Northern Railway	3,585.92	3,626.24	42,813.00	42,813.00
S.N.Ry.Bonds	- Other than Bonds held by The Western Pacific Railroad Company	45.38	-	544.90	-
	TOTAL	$62,255.49	$60,144.50	$743,529.71	$718,594.94

ORIGINAL
FILED

AUG 22 1942

with Clerk, U. S. Dist. Court
San Francisco

THE WESTERN PACIFIC RAILROAD COMPANY

SACRAMENTO NORTHERN RAILWAY

TIDEWATER SOUTHERN RAILWAY COMPANY

OPERATING RESULTS - COMBINED

(All Inter-Company Items Eliminated)

26591S

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ITEM OR ACCOUNT	MONTH OF JUNE				PERIOD JANUARY 1 TO JUNE 30			
	1942	1941	Increase or Decrease. Amount	Per Cent	1942	1941	Increase or Decrease. Amount	Per Cent
AVERAGE MILEAGE OF ROAD OPERATED	1,536.19	1,536.19	-	-	1,536.19	1,536.19	-	-
OPERATING REVENUES								
Freight	$ 2,569,699.19	$ 1,699,924.52	$ 869,774.67	51.17	$16,012,453.97	$ 9,498,738.47	$ 6,513,715.50	68.58
Passenger	178,827.21	98,875.60	80,951.61	81.87	798,653.14	383,987.48	414,665.66	107.99
Mail	3,000.00	3,000.00	-	-	17,986.87	18,012.29	(25.42)	(.14)
Express	37,540.02	15,352.56	22,187.46	144.52	72,201.29	41,929.82	30,271.47	72.20
Dining Car, Hotel & Restaurant	28,798.24	11,749.85	17,048.39	145.10	108,520.03	48,998.49	59,521.54	122.84
Miscellaneous	34,666.98	23,333.86	11,333.12	48.57	225,786.90	119,633.93	106,152.97	88.73
Total Railway Operating Revenues	$ 2,853,531.64	$ 1,852,236.39	$ 1,001,295.25	54.06	$16,235,600.20	$10,111,000.26	$ 6,124,601.92	60.57
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 314,121.66	$ 291,853.74	$ 22,267.92	7.63	$ 1,870,770.74	$ 1,445,419.45	$ 425,351.29	29.43
Maintenance of Equipment	380,778.55	340,050.32	40,728.23	11.98	2,213,640.73	1,788,863.93	424,786.80	23.75
Power	6,758.68	6,805.54	(46.86)	(.69)	44,064.86	44,106.32	(41.76)	(.09)
Traffic	75,011.62	73,814.82	1,803.20	1.63	466,100.69	428,663.50	37,437.39	8.73
Transportation - Rail Line	895,681.48	649,286.72	246,394.76	37.95	5,623,697.69	3,784,305.07	1,839,392.62	48.61
Miscellaneous Operations	28,311.55	13,907.42	14,404.13	103.57	121,088.83	67,621.09	53,464.64	79.06
General	75,572.79	66,565.24	9,007.55	13.53	450,113.58	361,924.88	88,188.70	17.85
Transportation for Investment - Credit	-	1,048.41	(1,048.41)	-	-	2,878.89	(2,878.89)	-
Total Railway Operating Expenses	$ 1,776,236.31	$ 1,446,235.39	$ 330,000.92	22.82	$10,789,673.72	$ 7,938,015.35	$ 2,851,658.37	35.92
NET REVENUE FROM RAILWAY OPERATIONS	$ 1,077,295.33	$ 406,001.00	$ 671,294.33	165.34	$ 5,445,926.48	$ 2,172,984.93	$ 3,272,943.55	150.62
Railway Tax Accruals - Payroll	$ 66,018.86	$ 49,886.18	$ 16,129.68	32.33	$ 408,466.37	$ 280,618.30	$ 127,846.98	45.56
Railway Tax Accruals - All Other	57,466.58	51,891.83	5,576.75	11.39	380,914.09	350,341.30	30,572.79	8.73
Railway Tax Accruals - Total	$ 123,484.44	$ 101,478.01	$ 22,006.43	21.69	$ 789,379.46	$ 630,959.60	$ 158,419.77	25.11
RAILWAY OPERATING INCOME	$ 953,810.89	$ 304,522.99	$ 649,287.90	213.21	$ 4,656,549.02	$ 1,542,025.34	$ 3,114,523.78	201.98
Equipment Rents - Net Debit	$ 116,313.23	$ 101,700.87	$ 14,612.36	14.37	$ 841,404.19	$ 627,365.00	$ 214,039.19	34.12
Joint Facility Rents - Net Credit	14,794.82	16,693.53	(1,898.71)	(11.37)	47,551.60	49,073.65	(842.03)	(1.13)
NET RAILWAY OPERATING INCOME	$ 852,292.48	$ 219,515.65	$ 632,776.83	288.26	$ 3,862,676.43	$ 968,733.87	$ 2,899,942.56	301.22
OTHER INCOME								
Rental of Property	$ 53,000.44	$ 32,289.42	$ 20,711.02	64.14	$ 292,322.23	$ 182,856.90	$ 109,468.33	59.87
Interest Accruals	1,747.30	3,440.37	(1,693.07)	(49.21)	10,933.13	19,688.73	(8,755.60)	(44.47)
Miscellaneous	167.89	11.00	156.89	-	3,237.30	919.31	2,317.99	252.14
Total Other Income	$ 54,915.63	$ 35,740.79	$ 19,174.84	53.65	$ 306,495.66	$ 203,464.94	$ 103,030.72	50.64
TOTAL INCOME	$ 907,208.11	$ 255,256.44	$ 651,951.67	255.41	$ 4,169,172.09	$ 1,166,198.81	$ 3,002,973.28	257.50
MISCELLANEOUS DEDUCTIONS FROM INCOME								
Miscellaneous Rents	$ 2,214.22	$ 2,189.16	$ 25.06	1.14	$ 13,988.06	$ 13,715.36	$ 272.70	1.84
Miscellaneous Tax Accruals	4,853.93	4,946.91	(92.98)	(1.88)	31,027.55	29,946.82	1,080.73	3.61
Miscellaneous	6,762.16	7,764.45	(1,002.29)	(12.91)	44,066.39	39,009.31	5,077.08	13.02
Total Miscellaneous Deductions	$ 13,830.31	$ 14,900.52	$ (1,070.21)	(7.18)	$ 89,081.99	$ 82,671.48	$ 6,410.51	7.75
INCOME AVAILABLE FOR FIXED CHARGES	$ 893,377.80	$ 240,355.92	$ 653,021.88	271.69	$ 4,080,090.10	$ 1,083,527.33	$ 2,996,562.77	276.56
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	-	-	$ 1,800.00	$ 1,800.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	205,375.41	205,375.41	-	-	1,232,252.50	1,232,252.50	-	-
Equipment Obligations do.	6,093.53	5,162.50	931.03	18.03	36,618.66	31,362.50	5,254.16	16.75
Trustees' Certificates do.	12,286.89	33,061.11	(20,772.22)	(62.83)	67,541.67	199,991.66	(111,449.99)	(56.01)
Other Obligations (*)	61,763.54	62,008.74	(245.20)	(.40)	371,064.11	370,945.24	108.87	.03
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	337.44	523.25	(185.81)	(35.51)	2,093.72	3,231.92	(1,138.20)	(35.22)
Other Obligations	26.21	80.20	(53.99)	(67.32)	1,822.41	233.75	1,588.66	12.79
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.49	11,283.49	-	-	67,700.94	67,700.94	-	-
Equipment Obligations do.	306.68	80.76	225.92	279.74	1,884.67	490.04	1,394.63	284.55
Total Fixed Charges	$ 297,775.19	$ 317,875.46	$ (20,100.27)	(6.33)	$ 1,802,999.83	$ 1,908,207.21	$ (105,207.38)	(5.53)
NET INCOME	$ 595,602.61	$ 77,519.54	$ 673,122.15	-	$ 2,277,090.27	$ 825,069.88	$ 3,102,160.43	-

Freight	$ 2,589,699.19	$ 1,699,924.52	$ 889,774.67	51.17	$16,212,453.97	$ 9,496,738.47	$ 5,513,715.50	58.06
Passenger	179,827.21	98,875.60	80,951.61	81.87	798,653.14	383,997.48	414,655.66	107.99
Mail	3,000.00	3,000.00	-	-	17,986.87	18,012.29	*25.42*	*.14*
Express	37,540.02	15,352.56	22,187.46	144.52	72,201.29	41,929.62	30,271.67	72.20
Dining Car, Hotel & Restaurant	28,798.24	11,749.85	17,048.39	145.10	108,520.03	48,686.49	59,821.54	122.84
Miscellaneous	34,666.98	23,333.12	11,333.12	48.57	225,786.90	119,633.93	106,152.97	88.73
Total Railway Operating Revenues	$ 2,853,531.64	$ 1,852,236.39	$ 1,001,295.25	54.06	$16,236,602.20	$10,111,000.28	$ 6,124,601.92	60.57
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 314,121.66	$ 291,853.74	$ 22,267.92	7.63	$ 1,870,770.74	$ 1,445,419.45	$ 425,351.29	29.43
Maintenance of Equipment	380,778.55	340,050.32	40,728.23	11.98	2,213,640.73	1,789,853.93	424,786.80	23.73
Power	6,788.66	6,805.54	*16.88*	*.69*	44,064.56	44,106.32	*41.76*	*.09*
Traffic	75,011.62	78,814.82	*3,803.20*	*4.83*	466,100.89	428,663.50	37,437.39	8.73
Transportation - Rail Line	895,681.48	649,286.72	246,394.76	37.95	5,823,697.89	3,784,308.07	1,839,389.82	48.61
Miscellaneous Operations	28,311.55	13,907.42	14,404.13	103.57	121,085.53	67,681.09	53,404.44	79.06
General	75,572.79	66,565.24	9,007.55	13.53	450,113.58	381,984.88	68,128.70	17.84
Transportation for Investment - Credit	-	1,048.41	*1,048.41*	-	-	2,878.89	*2,878.89*	-
Total Railway Operating Expenses	$ 1,776,236.31	$ 1,445,235.39	$ 330,000.92	22.82	$10,789,673.72	$ 7,938,015.35	$ 2,851,658.37	35.92
NET REVENUE FROM RAILWAY OPERATIONS	$ 1,077,295.33	$ 406,001.00	$ 671,294.33	165.34	$ 5,445,928.48	$ 2,172,984.93	$ 3,272,943.55	150.62
Railway Tax Accruals - Payroll	$ 66,015.85	$ 49,386.18	$ 16,129.68	32.33	$ 408,466.37	$ 280,418.39	$ 127,946.98	45.56
Railway Tax Accruals - All Other	57,468.58	51,891.83	5,576.75	11.39	360,914.09	360,241.30	50,672.79	8.73
Railway Tax Accruals - Total	$ 123,484.44	$ 101,278.01	$ 22,006.43	21.39	$ 769,379.46	$ 630,959.69	$ 188,419.77	25.11
RAILWAY OPERATING INCOME	$ 953,810.89	$ 304,522.99	$ 649,287.90	213.21	$ 4,656,549.02	$ 1,542,025.24	$ 3,114,523.78	201.96
Equipment Rents - Net Debit	$ 116,313.23	$ 101,700.87	$ 14,612.36	14.37	$ 841,404.19	$ 627,368.00	$ 214,039.19	34.12
Joint Facility Rents - Net Credit	14,794.82	16,693.53	*1,898.71*	*11.37*	47,531.60	48,073.63	*542.03*	*1.13*
NET RAILWAY OPERATING INCOME	$ 852,292.48	$ 219,515.65	$ 632,776.83	288.26	$ 3,862,676.43	$ 962,733.87	$ 2,899,942.56	301.22
OTHER INCOME								
Rental of Property	$ 53,000.44	$ 32,289.42	$ 20,711.02	64.14	$ 292,322.23	$ 182,856.90	$ 109,465.33	59.87
Interest Accruals	1,747.30	3,440.37	*1,693.07*	*49.21*	10,933.13	19,688.73	*8,755.60*	*44.47*
Miscellaneous	167.89	11.00	156.89	-	3,237.30	919.31	2,317.99	288.14
Total Other Income	$ 54,915.63	$ 35,740.79	$ 19,174.84	53.65	$ 306,495.66	$ 203,464.94	$ 103,030.72	50.64
TOTAL INCOME	$ 907,208.11	$ 255,256.44	$ 651,951.67	255.41	$ 4,169,172.09	$ 1,166,198.81	$ 3,002,973.28	257.50
MISCELLANEOUS DEDUCTIONS FROM INCOME								
Miscellaneous Rents	$ 2,214.22	$ 2,189.16	$ 25.06	1.14	$ 13,988.06	$ 13,715.35	$ 272.70	1.84
Miscellaneous Tax Accruals	4,853.93	4,946.91	*92.98*	*1.88*	31,027.86	29,946.88	1,080.73	3.61
Miscellaneous	6,762.16	7,764.45	*1,002.29*	*13.91*	44,086.39	39,009.31	5,077.08	13.02
Total Miscellaneous Deductions	$ 13,830.31	$ 14,900.52	$ *1,070.21*	*7.18*	$ 89,081.99	$ 82,671.48	$ 6,410.51	7.75
INCOME AVAILABLE FOR FIXED CHARGES	$ 893,377.80	$ 240,355.92	$ 653,021.88	271.69	$ 4,080,090.10	$ 1,083,527.33	$ 2,996,562.77	276.56
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	-	-	$ 1,800.00	$ 1,800.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	206,375.41	206,375.41	-	-	1,232,252.50	1,232,252.50	-	-
Equipment Obligations do.	6,093.53	5,162.50	931.03	18.03	36,616.66	31,332.50	5,284.16	16.75
Trustees' Certificates do.	12,288.89	33,061.11	*20,772.22*	*62.83*	87,641.97	198,991.66	*111,449.99*	*56.01*
Other Obligations (*)	61,763.54	62,006.74	*243.20*	*.40*	371,054.11	370,945.24	108.87	.03
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	337.44	523.25	*185.81*	*35.51*	2,093.72	3,231.92	*1,138.20*	*35.22*
Other Obligations	26.21	80.20	*53.99*	*67.32*	2,056.46	1,822.41	233.75	12.79
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.49	11,283.49	-	-	67,700.94	67,700.94	-	-
Equipment Obligations do.	306.68	80.76	225.92	279.74	1,884.47	480.04	1,384.43	284.55
Total Fixed Charges	$ 297,775.19	$ 317,875.46	$ *20,100.27*	*6.32*	$ 1,802,999.83	$ 1,908,887.21	$ *105,887.38*	*5.53*
NET INCOME	$ 595,602.61	$ *77,519.54*	$ 673,122.15	-	$ 2,277,090.27	$ *825,069.88*	$ 3,102,160.45	-

NOTE - Itálics denote Red

Note (*) - "Interest on Funded Debt - Other obligations" includes the following:

		Month		Period	
		1942	1941	1942	1941
Notes Payable	- Reconstruction Finance Corporation	$ 12,176.71	$ 12,176.71	$ 73,466.16	$ 73,466.16
do.	- A. C. James Co.	20,832.50	20,832.50	124,995.00	124,995.00
do.	- Railroad Credit Corporation	2,036.01	2,036.01	12,216.06	12,216.06
Advances	- The Western Pacific Railroad Corporation	22,894.80	22,894.80	137,368.05	137,368.05
do.	- The Western Realty Company	208.35	208.35	1,250.00	1,250.00
do.	- The Western Pacific Railroad Corporation to Sacramento Northern Railway	3,567.75	3,566.90	21,406.50	21,397.58
S.N.Ry. Bonds	- Other than held by The W.P.R.R.Co.	45.42	272.47	272.42	272.47
	TOTAL:	$ 61,763.54	$ 62,008.74	$371,054.11	$370,945.24

Accounting Department
San Francisco, California
August 12, 1942.

THE WESTERN PACIFIC RAILROAD COMPANY

SACRAMENTO NORTHERN RAILWAY

TIDEWATER SOUTHERN RAILWAY COMPANY

OPERATING RESULTS - COMBINED

(All Inter-Company Items Eliminated)

ITEM OR ACCOUNT	MONTH OF JULY				PERIOD JANUARY 1 TO JULY 31			
	1942	1941	Increase or Decrease. Amount	Per Cent	1942	1941	Increase or Decrease. Amount	Per Cent
AVERAGE MILEAGE OF ROAD OPERATED	1,536.19	1,536.19	-	-	1,536.19	1,536.19	-	-
OPERATING REVENUES								
Freight	$ 2,796,294.30	$ 1,932,800.89	$ 863,493.41	44.68	$17,807,678.27	$11,431,539.36	$ 6,376,138.91	55.78
Passenger	187,680.40	83,383.11	104,297.09	125.01	988,373.54	467,370.79	518,902.75	111.03
Mail	3,000.00	3,000.00	000.00	0.07	21,186.67	21,012.29	174.38	.83
Express	16,560.97	5,549.73	11,080.24	199.67	88,771.96	47,479.35	41,291.91	86.97
Dining Car, Hotel & Restaurant	28,908.41	14,186.47	12,722.94	89.68	135,488.44	62,883.98	72,544.46	115.36
Miscellaneous	53,996.49	33,386.98	20,609.51	61.73	279,783.39	153,080.91	126,702.48	82.84
Total Railway Operating Revenues	$ 3,083,519.57	$ 2,072,306.38	$ 1,011,213.19	48.80	$19,319,181.77	$12,183,306.66	$ 7,135,875.11	58.57
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 355,228.27	$ 309,285.93	$ 45,942.34	14.85	$ 2,226,009.01	$ 1,754,715.38	$ 471,293.63	26.86
Maintenance of Equipment	370,272.67	351,906.80	18,366.87	5.22	2,583,913.50	2,140,729.73	443,183.47	20.70
Power	6,994.72	8,253.54	*1,258.82*	*15.10*	50,989.88	52,360.86	*1,370.58*	*2.62*
Traffic	80,318.13	74,537.77	5,774.36	7.75	546,413.02	503,201.27	43,211.75	8.59
Transportation - Rail Line	977,753.12	692,776.77	284,976.35	41.14	6,601,580.81	4,477,081.84	2,124,498.97	47.46
Miscellaneous Operations	28,098.05	15,489.03	12,609.02	81.41	149,183.88	83,110.12	66,073.46	79.50
General	78,827.87	61,560.69	17,067.18	27.72	588,741.45	443,686.87	85,255.88	19.22
Transportation for Investment - Credit	33.82	297.70	*263.88*	*88.64*	33.82	3,176.99	*3,142.77*	*98.94*
Total Railway Operating Expenses	$ 1,897,198.81	$ 1,513,821.83	$ 383,370.98	25.38	$12,696,856.53	$ 9,481,637.19	$ 3,236,389.36	34.23
NET REVENUE FROM RAILWAY OPERATIONS	$ 1,186,320.76	$ 558,784.55	$ 627,848.21	112.30	$ 6,622,325.24	$ 2,731,769.48	$ 3,900,488.76	142.78
Railway Tax Accruals - Payroll	$ 74,914.72	$ 52,268.28	$ 22,646.44	43.33	$ 483,160.09	$ 338,715.93	$ 150,464.16	44.20
Railway Tax Accruals - All Other	334,243.86	103,316.78	230,927.80	223.82	715,187.74	453,687.79	261,499.95	57.65
Railway Tax Accruals - Total	$ 409,158.57	$ 155,584.03	$ 253,574.54	162.98	$ 1,198,537.83	$ 792,543.72	$ 411,994.11	52.00
RAILWAY OPERATING INCOME	$ 777,162.19	$ 403,200.52	$ 373,967.67	92.75	$ 5,423,717.41	$ 1,948,225.76	$ 3,488,491.65	179.14
Equipment Rents - Net Debit	$ 141,731.53	$ 125,262.56	$ 16,468.97	13.15	$ 983,135.72	$ 752,627.56	$ 230,508.16	30.63
Joint Facility Rents - Net Credit	30,174.55	8,194.17	11,980.36	146.21	87,706.15	56,967.80	11,438.35	20.33
NET RAILWAY OPERATING INCOME	$ 665,611.41	$ 286,132.13	$ 369,479.28	129.13	$ 4,518,287.94	$ 1,248,886.00	$ 3,269,421.94	261.79
OTHER INCOME								
Rental of Property	$ 57,614.86	$ 34,320.05	$ 23,294.81	67.88	$ 349,940.09	$ 217,176.95	$ 132,763.14	61.13
Interest Accruals	1,789.30	3,488.53	*1,699.23*	*49.13*	12,692.43	23,147.26	*10,454.83*	*45.17*
Miscellaneous	46,719.70	46.00	46,674.70	-	49,987.00	964.31	49,022.69	-
Total Other Income	$ 106,093.86	$ 37,823.58	$ 68,270.28	180.50	$ 412,599.52	$ 241,288.52	$ 171,301.00	70.99
TOTAL INCOME	$ 761,706.27	$ 323,966.71	$ 437,749.56	135.13	$ 4,930,877.36	$ 1,490,154.52	$ 3,440,722.84	230.90
MISCELLANEOUS DEDUCTIONS FROM INCOME								
Miscellaneous Rents	$ 2,199.23	$ 2,174.17	$ 25.06	1.15	$ 16,167.23	$ 15,889.52	$ 277.76	1.75
Miscellaneous Tax Accruals	5,486.80	5,075.25	351.25	6.92	36,454.05	35,022.07	1,431.98	4.09
Miscellaneous	3,272.90	5,111.67	*1,838.77*	*35.97*	47,309.29	44,120.98	3,238.31	7.34
Total Miscellaneous Deductions	$ 10,998.93	$ 12,361.09	$ *1,462.46*	*11.83*	$ 99,980.82	$ 95,032.57	$ 4,948.05	5.21
INCOME AVAILABLE FOR FIXED CHARGES	$ 750,806.64	$ 311,894.62	$ 439,212.02	140.98	$ 4,830,896.74	$ 1,395,121.95	$ 3,435,774.79	246.27
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	$ -	-	$ 2,100.00	$ 2,100.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	205,375.41	205,375.41	-	-	1,437,627.91	1,437,627.91	-	-
Equipment Obligations do.	6,093.54	5,162.50	931.04	18.03	42,710.20	36,525.00	6,185.20	16.93
Trustees' Certificates do. (A)	12,206.56	33,019.44	*20,813.88*	*63.04*	99,747.23	232,011.10	*132,263.87*	*57.01*
Other Obligations (e)	62,237.14	62,256.29	*18.15*	*.03*	433,291.35	433,200.53	90.72	.02
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	328.81	413.02	*80.21*	*19.42*	2,426.53	3,644.94	*1,218.41*	*33.43*
Other Obligations	60.49	356.86	*296.37*	*83.05*	2,115.95	2,179.27	*63.32*	*2.91*
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.69	11,283.69	-	-	78,984.43	78,984.43	-	-
Equipment Obligations do.	315.10	80.76	234.34	290.17	2,199.87	570.50	1,629.37	285.35
Total Fixed Charges	$ 298,903.54	$ 318,246.77	$ *20,043.23*	*6.30*	$ 2,101,203.07	$ 2,226,843.98	*125,640.91*	*5.64*
NET INCOME	$ 452,603.10	$ *6,652.15*	$ 459,255.25	-	$ 2,729,693.67	$ *831,722.03*	$ 3,561,415.70	-

NOTE - Italics denote red.

Freight	$ 2,798,224.30	$ 1,932,800.89	$ 882,423.41	44.82	$17,807,676.27	$11,431,539.36	$ 6,376,136.91	55.78
Passenger	187,280.40	83,383.31	104,237.09	125.01	986,573.54	467,370.79	518,902.75	111.03
Mail	3,000.00	3,000.00	200.00	6.67	21,186.87	21,012.29	174.58	.83
Express	16,569.97	5,549.73	11,020.24	198.57	89,771.96	47,479.35	41,291.61	86.97
Dining Car, Hotel & Restaurant	28,908.41	14,186.47	12,722.94	89.69	136,428.44	62,883.98	72,544.46	115.36
Miscellaneous	53,996.49	33,386.98	20,609.51	61.73	279,783.39	153,090.91	126,692.48	82.84
Total Railway Operating Revenues	$ 3,088,819.87	$ 2,072,306.38	$ 1,011,213.19	48.80	$19,319,121.77	$12,183,306.66	$ 7,135,815.11	58.57
OPERATING EXPENSES								
Maintenance of Way & Structures	$ 355,239.87	$ 309,295.93	$ 45,943.94	14.85	$ 2,226,009.01	$ 1,754,715.38	$ 471,293.63	26.86
Maintenance of Equipment	370,272.47	351,905.80	18,366.67	5.22	2,583,913.20	2,140,729.73	443,183.47	20.70
Power	6,994.72	8,283.54	*1,328.82*	*16.10*	50,989.88	52,360.26	*1,370.38*	*2.62*
Traffic	80,312.13	74,537.77	5,774.36	7.75	546,413.02	503,201.27	43,211.75	8.59
Transportation - Rail Line	977,753.12	692,776.77	284,976.35	41.14	6,601,550.81	4,477,081.84	2,124,468.97	47.45
Miscellaneous Operations	26,090.05	10,489.03	12,600.02	61.41	149,183.58	83,110.12	66,073.46	79.50
General	78,627.87	61,560.69	17,067.18	27.72	588,741.45	443,486.87	85,256.58	19.22
Transportation for Investment - Credit	33.82	297.70	*263.88*	*88.64*	33.82	3,176.99	*3,143.17*	*98.94*
Total Railway Operating Expenses	$ 1,897,198.81	$ 1,513,821.83	$ 383,970.98	25.36	$12,696,986.53	$ 9,451,837.19	$ 3,236,389.36	34.23
NET REVENUE FROM RAILWAY OPERATIONS	$ 1,196,326.76	$ 548,794.85	$ 627,548.21	118.30	$ 6,628,235.24	$ 2,731,769.48	$ 3,900,465.76	142.78
Railway Tax Accruals - Payroll	$ 74,914.72	$ 52,968.88	$ 22,646.44	43.33	$ 683,360.09	$ 338,918.93	$ 180,464.16	45.20
Railway Tax Accruals - All Other	334,943.85	103,316.75	230,227.30	223.52	715,167.74	453,667.79	261,499.95	57.65
Railway Tax Accruals - Total	$ 409,138.37	$ 156,284.03	$ 253,874.34	162.98	$ 1,198,837.83	$ 792,543.72	$ 411,994.11	52.36
RAILWAY OPERATING INCOME	$ 777,188.39	$ 402,800.86	$ 373,987.87	92.78	$ 5,433,717.41	$ 1,945,225.76	$ 3,488,491.98	179.34
Equipment Rents - Net Debit	$ 141,731.53	$ 125,262.86	$ 16,468.67	13.15	$ 983,135.72	$ 732,627.86	$ 250,508.16	30.65
Joint Facility Rents - Net Credit	20,174.55	9,294.17	11,980.38	146.21	67,736.15	56,267.80	11,439.25	20.33
NET RAILWAY OPERATING INCOME	$ 655,611.41	$ 286,132.13	$ 369,479.28	129.13	$ 4,518,287.84	$ 1,268,865.00	$ 3,249,321.84	261.79
OTHER INCOME								
Rental of Property	$ 87,614.86	$ 54,280.08	$ 33,294.81	97.86	$ 349,940.09	$ 217,176.95	$ 132,763.14	61.13
Interest Accruals	1,789.30	3,468.53	*1,699.23*	*49.13*	12,922.43	23,147.26	*10,454.83*	*45.17*
Miscellaneous	46,719.70	46.00	46,674.70	-	49,987.00	964.31	48,992.69	-
Total Other Income	$ 106,083.86	$ 57,823.88	$ 48,270.28	180.50	$ 412,869.82	$ 241,288.52	$ 171,301.00	70.99
TOTAL INCOME	$ 761,705.27	$ 323,955.71	$ 437,749.56	135.13	$ 4,930,877.36	$ 1,490,154.52	$ 3,440,722.84	230.90
MISCELLANEOUS DEDUCTIONS FROM INCOME								
Miscellaneous Rents	$ 2,199.23	$ 2,174.17	$ 25.06	1.15	$ 16,187.25	$ 15,889.52	$ 277.76	1.75
Miscellaneous Tax Accruals	5,426.50	5,075.25	351.25	6.92	36,454.05	35,022.07	1,431.98	4.09
Miscellaneous	3,272.90	5,111.67	*1,838.77*	*35.97*	47,359.29	44,120.98	3,238.31	7.34
Total Miscellaneous Deductions	$ 10,898.63	$ 12,361.09	*$ 1,462.46*	*11.83*	$ 99,980.62	$ 95,032.57	$ 4,948.05	5.21
INCOME AVAILABLE FOR FIXED CHARGES	$ 750,806.64	$ 311,594.62	$ 439,212.02	140.96	$ 4,830,896.74	$ 1,395,121.95	$ 3,435,774.79	246.27
FIXED CHARGES								
Rent for Leased Roads and Equipment	$ 300.00	$ 300.00	$ -	-	$ 2,100.00	$ 2,100.00	$ -	-
Interest on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	205,375.41	205,375.41	-	-	1,437,627.91	1,437,627.91	-	-
Equipment Obligations do.	6,093.54	5,162.50	931.04	18.03	42,710.20	36,585.00	6,125.20	16.93
Trustees' Certificates do. (A)	12,206.56	33,019.44	*20,813.88*	*63.04*	99,747.23	232,011.10	*132,263.87*	*57.01*
Other Obligations (*)	68,237.14	68,255.29	*18.15*	*.03*	433,291.25	433,200.53	90.72	.02
Interest on Unfunded Debt:								
Equipment Obligations (W.P.R.R.Co.)	338.81	413.02	*80.21*	*19.42*	2,426.53	3,644.94	*1,218.41*	*33.43*
Other Obligations	80.69	386.86	*306.37*	*83.08*	2,115.96	2,179.27	*63.32*	*2.91*
Amortization of Discount on Funded Debt:								
First Mortgage Bonds (W.P.R.R.Co.)	11,283.49	11,283.49	-	-	78,984.43	78,984.43	-	-
Equipment Obligations do.	318.10	80.76	*234.34*	*290.17*	2,199.87	570.80	*1,629.77*	*285.56*
Total Fixed Charges	$ 306,203.84	$ 318,246.77	*$ 20,043.23*	*6.30*	$ 2,101,203.07	$ 2,226,843.98	*125,640.91*	*5.64*
NET INCOME	$ 452,603.10	$ *6,652.15*	$ 459,255.25	-	$ 2,729,693.67	$ *831,722.03*	$ 3,561,415.70	-

NOTE - Italics denote red.

(A) Excluding interest on cash collateral deposited with Reconstruction Finance Corporation, as follows:

$5,000,000.00 December 1, 1941.
1,000,000.00 April 24, 1942.

Note (*) - "Interest on Funded Debt - Other Obligations" includes the following:

		Month		Period	
		1942	1941	1942	1941
Notes Payable	- Reconstruction Finance Corp.	$ 12,582.61	$ 12,582.61	$ 86,048.77	$ 86,048.77
do.	- A. C. James Co.	20,832.50	20,832.50	145,827.50	145,827.50
do.	- Railroad Credit Corp.	2,106.94	2,106.94	14,401.92	14,401.92
Advances	- The Western Pacific Railroad Corp.	22,894.65	22,894.65	160,262.70	160,262.70
do.	- The Western Realty Co.	208.32	208.32	1,458.32	1,458.32
do.	- The Western Pacific Railroad Corp. to Sacramento Northern Railway	3,867.78	3,585.90	24,974.25	24,883.48
S.N.Ry. Bonds	- Other than held by The Western Pacific Railroad Co.	45.37	45.37	317.79	317.84
	TOTAL:	$ 68,237.14	$ 68,255.29	$433,291.25	$433,200.53

Accounting Department
San Francisco, California
September 16, 1942.

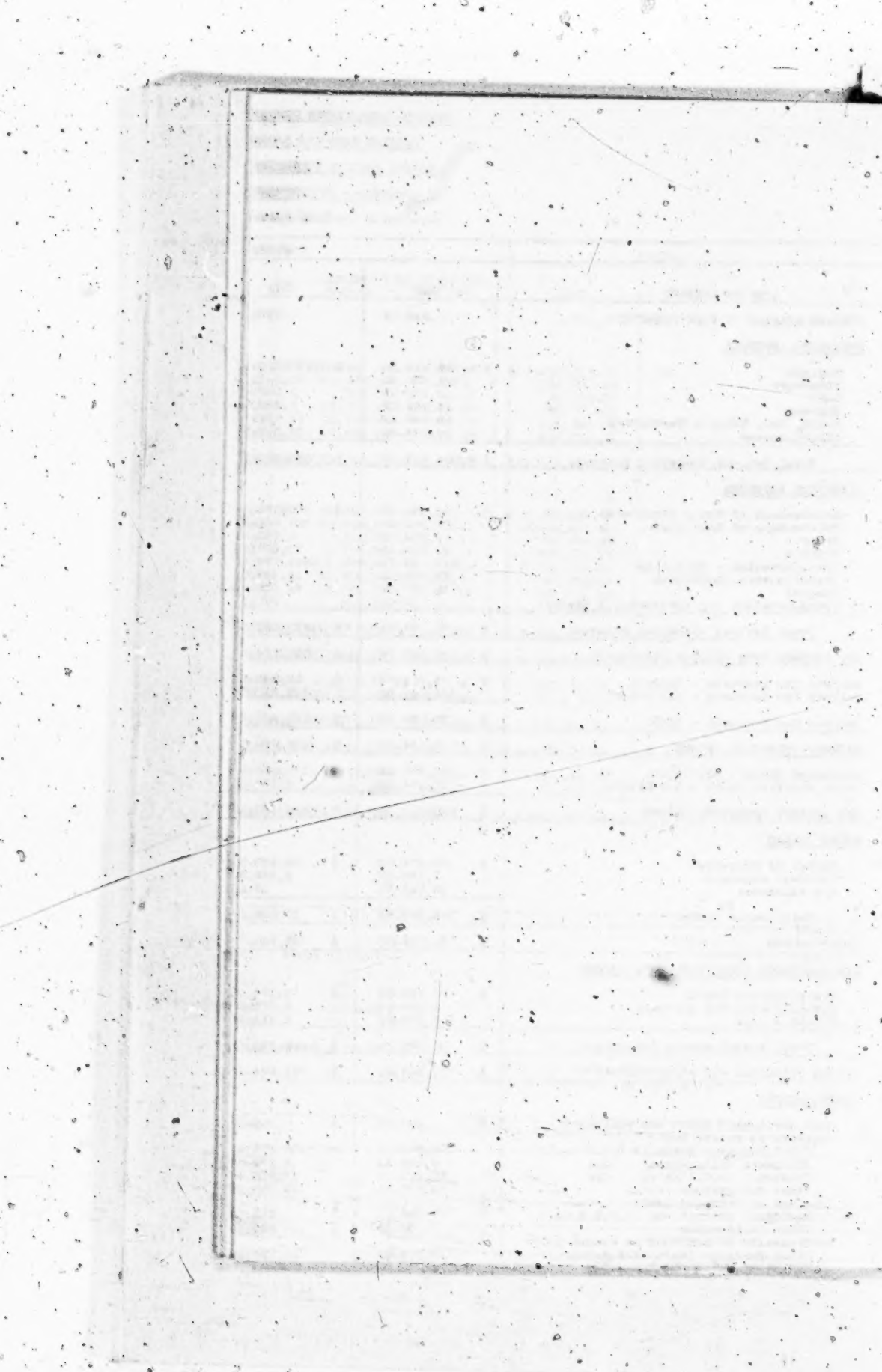

Exhibit L

Total Operating Revenues
of
THE WESTERN PACIFIC RAILROAD SYSTEM (‡)
and
CLASS I RAILROADS OF THE UNITED STATES (†)
(Revenues shown in Thousands)

ASSUMED "NORMAL" PERIOD

	Class I Railroads of United States (†)		The Western Pacific System	
	Revenues (000)	% of Assumed Normal Period	Revenues (000)	% of Assumed Normal Period
1923	$6,289,580	101.92%	$14,415	88.72%
1924	5,921,496	95.96	14,669	90.28
1925	6,122,509	99.22	15,899	97.85
1926	6,382,939	103.44	17,951	110.48
1927	6,136,300	99.44	18,306	112.67
5-Yr. Av.	$6,170,565	100.00%	$16,248	100.00%

AFTER ASSUMED "NORMAL" PERIOD

	Class I Railroads of United States (†)		The Western Pacific Railroad System (‡)				
	Revenues (000)	% of Assumed Normal Period	W. P. Excl. N.C.E. Revenues (000)	% of Assumed Normal Period	Add'l for N.C.E. (*) (000)	W. P. Incl. N.C.E. Revenues (000)	% of Assumed Normal Period
1928	$6,111,735	99.04%	$19,422	119.53	$	$	%
1929	6,279,521	101.76	20,097	123.69			
1930	5,281,197	85.58	18,819	115.82			
1931	4,188,343	67.87	14,688	90.40	165	14,853	91.41
1932	3,126,760	50.67	11,018	67.81	1,233	12,251	75.40
1933	3,095,404	50.16	10,711	65.92	1,491	12,202	75.10
1934	3,271,566	53.02	11,660	71.76	2,119	13,779	84.80
1935	3,451,929	55.94	12,117	74.58	2,290	14,407	88.67
1936	4,052,734	65.68	13,395	82.44	3,152	16,547	101.84
1937	4,166,069	67.52	14,492	89.19	3,426	17,918	110.28
1938	3,565,491	57.78	12,963	79.78	3,094	16,057	98.82

Source:—Class I revenues 1923-1937 taken from I. C. C. Statistics of Railways, and 1938 revenues taken from Bureau of Railway Economics statements.

(‡) The Western Pacific Railroad System is comprised of
The Western Pacific R.R. Co.,
Sacramento Northern Railway,
Tidewater Southern Railway Co.,
Deep Creek Railroad Company.

(†) Excludes Switching and Terminal Companies.

(*) Northern California Extension (NCE) placed in freight service Nov. 10, 1931.